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

FORM 10-Q

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

For the quarterly period ended September 30, 2003

Commission File Number 1-3924

MAXXAM INC.
(Exact name of Registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-2078752** (I.R.S. Employer Identification Number)
5847 San Felipe, Suite 2600 **Houston, Texas** (Address of Principal Executive Offices)	**77057** (Zip Code)

Registrant's telephone number, including area code: **(713) 975-7600**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes ☐ No ☒

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, as of the last business day of the registrant's most recently completed second fiscal quarter: $52.8 million.

Number of shares of common stock outstanding at November 13, 2003: 6,192,371

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MAXXAM INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET
(In millions of dollars, except share information)

	September 30, 2003 (Unaudited)	December 31, 2002
Assets		
Current assets:		
Cash and cash equivalents	$ 30.1	$ 45.6
Marketable securities	121.5	105.7
Receivables:		
Trade, net of allowance for doubtful accounts of $2.8 and $2.9, respectively	12.6	11.4
Other	3.0	4.6
Inventories:		
Lumber	20.2	22.2
Logs	10.4	12.4
Prepaid expenses and other current assets	41.1	41.8
Total current assets	238.9	243.7
Property, plant and equipment, net of accumulated depreciation of $158.9 and $140.4, respectively	365.8	375.2
Timber and timberlands, net of accumulated depletion of $212.0 and $204.5, respectively	220.9	227.3
Deferred income taxes	83.5	82.4
Restricted cash, marketable securities and other investments	45.3	63.6
Long-term receivables and other assets	109.6	115.1
	$ 1,064.0	$ 1,107.3
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	$ 12.2	$ 12.2
Accrued interest	12.2	26.0
Accrued compensation and related benefits	15.4	14.0
Other accrued liabilities	20.4	27.6
Short-term borrowings and current maturities of long-term debt, excluding $4.0 and $2.6, respectively, of repurchased Timber Notes held in the SAR Account	50.9	30.5
Total current liabilities	111.1	110.3
Long-term debt, less current maturities and excluding $52.6 and $52.8, respectively, of repurchased Timber Notes held in the SAR Account	955.1	982.3
Accrued postretirement medical benefits	10.6	10.3
Losses in excess of investment in Kaiser	516.2	516.2
Other noncurrent liabilities	78.2	70.7
Total liabilities	1,671.2	1,689.8
Commitments and contingencies (see Note 8)		
Stockholders' deficit:		
Preferred stock, $0.50 par value; $0.75 liquidation preference; Class A $0.05 Non-Cumulative Participating Convertible Preferred Stock; 12,500,000 shares authorized; 669,235 shares issued; 668,390 shares outstanding	0.3	0.3
Common stock, $0.50 par value; 28,000,000 shares authorized; 10,063,359 shares issued; 6,513,071 and 6,527,671 shares outstanding, respectively	5.0	5.0
Additional capital	225.3	225.3
Accumulated deficit	(633.1)	(608.2)
Accumulated other comprehensive loss	(88.8)	(89.2)
Treasury stock, at cost (shares held: preferred – 845; common – 3,550,288 and 3,535,688, respectively)	(115.9)	(115.7)
Total stockholders' deficit	(607.2)	(582.5)
	$ 1,064.0	$ 1,107.3

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

MAXXAM INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS
(In millions of dollars, except per share information)

	Three Months Ended September 30, 2003	Three Months Ended September 30, 2002	Nine Months Ended September 30, 2003	Nine Months Ended September 30, 2002
	(Unaudited)			
Net sales:				
Forest products	$ 56.1	$ 51.8	$ 156.6	$ 154.0
Real estate	20.4	13.7	48.7	37.8
Racing	7.7	8.1	22.0	23.0
Aluminum	–	–	–	167.5
	84.2	73.6	227.3	382.3
Costs and expenses:				
Cost of sales and operations:				
Forest products	38.4	32.3	106.2	103.8
Real estate	5.8	4.5	18.0	14.7
Racing	5.4	5.5	15.3	15.0
Aluminum	–	–	–	158.6
Selling, general and administrative expenses	15.3	17.7	45.3	69.4
Impairment of assets	1.4	–	1.4	–
Depreciation, depletion and amortization	9.1	8.8	27.9	36.3
	75.4	68.8	214.1	397.8
Operating income (loss):				
Forest products	6.7	5.4	16.0	15.3
Real estate	4.9	1.9	4.3	0.7
Racing	(0.7)	(0.5)	(1.3)	0.2
Aluminum	–	–	–	(23.6)
Corporate	(2.1)	(2.0)	(5.8)	(8.1)
	8.8	4.8	13.2	(15.5)
Other income (expense):				
Investment, interest and other income (expense), net	3.9	2.9	19.8	10.7
Interest expense	(18.5)	(18.9)	(56.3)	(70.3)
Amortization of deferred financing costs	(0.5)	(0.8)	(1.6)	(2.6)
Loss before income taxes and minority interests	(6.3)	(12.0)	(24.9)	(77.7)
Income tax benefit	–	4.6	–	7.4
Minority interests	–	–	–	0.9
Net loss	$ (6.3)	$ (7.4)	$ (24.9)	$ (69.4)
Basic and diluted loss per common and common equivalent share	$ (0.96)	$ (1.14)	$ (3.81)	$ (10.64)

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

MAXXAM INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS
(In millions of dollars)

	Nine Months Ended September 30, 2003	Nine Months Ended September 30, 2002
	(Unaudited)	
Cash flows from operating activities:		
Net loss	$ (24.9)	$ (69.4)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation, depletion and amortization	27.9	36.3
Net gains on asset dispositions	(0.9)	(4.8)
Net gains on marketable securities	(13.5)	(1.8)
Minority interests	–	(0.9)
Amortization of deferred financing costs	1.6	2.6
Equity in (earnings) loss of unconsolidated affiliates, net of dividends received	(1.2)	1.3
Increase (decrease) in cash resulting from changes in:		
Receivables	2.0	21.6
Inventories	3.4	15.7
Prepaid expenses and other current assets	1.2	45.2
Accounts payable	0.6	9.8
Accrued and deferred income taxes	–	(13.2)
Payable to affiliates and other accrued liabilities	(2.8)	(44.9)
Accrued interest	(13.8)	(7.8)
Long-term assets and long-term liabilities	4.8	(29.2)
Other	0.9	0.2
Net cash used for operating activities	(14.7)	(39.3)
Cash flows from investing activities:		
Net proceeds from dispositions of property and investments	3.5	6.5
Net sales of marketable securities and other investments	1.2	7.6
Capital expenditures	(14.5)	(17.5)
Decrease in cash attributable to deconsolidation of Kaiser	–	(130.4)
Other	0.3	0.3
Net cash used for investing activities	(9.5)	(133.5)
Cash flows from financing activities:		
Proceeds from issuances of long-term debt	1.2	6.8
Redemptions, repurchases of and principal payments on long-term debt	(24.4)	(61.1)
Borrowings (repayments) under revolving and short-term credit facilities	20.3	(14.5)
Restricted cash withdrawals, net	11.8	30.4
Other	(0.2)	(1.3)
Net cash provided by (used for) financing activities	8.7	(39.7)
Net decrease in cash and cash equivalents	(15.5)	(212.5)
Cash and cash equivalents at beginning of period	45.6	272.2
Cash and cash equivalents at end of period	$ 30.1	$ 59.7
Supplemental disclosure of cash flow information:		
Interest paid, net of capitalized interest	$ 70.1	$ 78.2

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

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The information contained in the following notes to the consolidated financial statements is condensed from that which would appear in the annual consolidated financial statements; accordingly, the consolidated financial statements included herein should be reviewed in conjunction with the consolidated financial statements and related notes thereto contained in the Form 10-K. Any capitalized terms used but not defined in these Condensed Notes to Consolidated Financial Statements are defined in the "Glossary of Defined Terms" contained in Appendix A. All references to the "Company" include MAXXAM Inc. and its majority and wholly owned subsidiaries (but exclusive of Kaiser and its subsidiaries), unless otherwise indicated or the context indicates otherwise. All references to "Kaiser," "MGHI," "Pacific Lumber," "MPC" and "SHRP, Ltd." refer to the respective companies and their subsidiaries, unless otherwise indicated or the context indicates otherwise. Accounting measurements at interim dates inherently involve greater reliance on estimates than at year end. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the entire year.

The consolidated financial statements included herein are unaudited; however, they include all adjustments of a normal recurring nature which, in the opinion of management, are necessary for a fair presentation of the consolidated financial position of the Company at September 30, 2003, the consolidated results of operations for the three and nine months ended September 30, 2003 and 2002, and the consolidated cash flows for the nine months ended September 30, 2003 and 2002.

Reclassifications

The adoption of SFAS No. 145 in January 2003 resulted in the inclusion of $0.3 million and $3.5 million of gains on repurchases of debt for the three and nine month periods ended September 30, 2002, respectively, in investment, interest and other income rather than as extraordinary items in the accompanying financial statements (see Note 2).

Deconsolidation of Kaiser

Under generally accepted accounting principles, consolidation is generally required for investments of more than 50% of the outstanding voting stock of an investee, except when control is not held by the majority owner. Under these rules, legal reorganization or bankruptcy represent conditions which can preclude consolidation in instances where control rests with the bankruptcy court, rather than the majority owner. As discussed below, on February 12, 2002, Kaiser and certain of its subsidiaries filed for reorganization under Chapter 11 of the Code. As a result, the Company discontinued consolidating Kaiser's financial results beginning February 12, 2002, and the Company began reporting its investment in Kaiser using the cost method, under which the investment is reflected as a single amount on the Company's balance sheet of $(516.2) million, and the recording of earnings or losses from Kaiser was discontinued after February 11, 2002.

Through February 11, 2002, under generally accepted principles of consolidation, the Company had recognized losses in excess of its investment in Kaiser of $516.2 million. Since Kaiser's results are no longer consolidated and the Company believes that it is not probable that it will be obligated to fund losses related to its investment in Kaiser, any adjustments reflected in Kaiser's financial statements subsequent to February 12, 2002 (relating to the recoverability and classification of recorded asset amounts and classification of liabilities or the effects on existing stockholders' deficit as well as adjustments made to Kaiser's financial information for loss contingencies and other matters), are not expected to affect the Company's financial results.

The Company expects it will consider reversal of its losses in excess of its investment in Kaiser when either: (1) Kaiser's bankruptcy is resolved and the amount of the Company's remaining investment in Kaiser is determined or (2) the Company disposes of its shares of Kaiser common stock. Accordingly, these consolidated financial statements do not reflect any adjustments related to the deconsolidation of Kaiser other than presenting the Company's investment in Kaiser using the cost method. When either of the events described above occurs, the Company will re-evaluate the appropriate accounting treatment of its investment in Kaiser based upon the facts and circumstances at such time. It is likely that the Company's ownership interest in Kaiser will be cancelled. See Note 5 for further discussion of the Company's investment in Kaiser.

The following financial information is presented for comparison purposes. The financial information for the nine months ended September 30, 2002, is condensed pro forma financial information which reflects the results of operations of the Company excluding Kaiser (in millions, except share data).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net sales	$ 84.2	$ 73.6	$ 227.3	$ 214.8
Costs and expenses	(75.4)	(68.8)	(214.1)	(206.7)
Operating income	8.8	4.8	13.2	8.1
Other income (expenses), net	3.9	2.9	19.8	18.8
Interest expense and amortization of deferred financing costs	(19.0)	(19.7)	(57.9)	(60.2)
Loss before income taxes	(6.3)	(12.0)	(24.9)	(33.3)
Income tax benefit	–	4.6	–	12.1
Minority interests	–	–	–	0.2
Net loss	$ (6.3)	$ (7.4)	$ (24.9)	$ (21.0)
Basic and diluted loss per share	$ (0.96)	$ (1.14)	$ (3.81)	$ (3.22)

2. New Accounting Standards

Accounting for Asset Retirement Obligations

In January 2003, the Company adopted SFAS No. 143, which addresses accounting and reporting standards for obligations associated with the retirement of tangible long-lived assets and the related asset retirement costs. In general, SFAS No. 143 requires the recognition of a liability resulting from anticipated asset retirement obligations, offset by an increase in the value of the associated productive asset for such anticipated costs. Over the life of the asset, depreciation expense is to include the ratable expensing of the retirement cost included with the asset value. The statement applies to all legal obligations associated with the retirement of a tangible long-lived asset that result from the acquisition, construction, or development and/or the normal operation of a long-lived asset, except for certain lease obligations. Excluded from this Statement are obligations arising solely from a plan to dispose of a long-lived asset and obligations that result from the improper operation of an asset (i.e. certain types of environmental obligations). The adoption of SFAS No. 143 did not have a material impact on the Company’s financial position or results of operations.

Classification of Gains and Losses from Extinguishment of Debt

In January 2003, the Company adopted SFAS No. 145, which, among other things, rescinds the previous guidance for debt extinguishments. SFAS No. 145 eliminates the requirement that gains and losses from extinguishment of debt be aggregated and, if material, classified as an extraordinary item, net of related income tax effect. However, transactions would not be prohibited from extraordinary item classification if they meet the criteria in APB Opinion No. 30. Applying the provisions of APB Opinion No. 30 will distinguish transactions that are part of an entity’s recurring operations from those that are unusual or infrequent or that meet the criteria for classification as an extraordinary item. The adoption of SFAS No. 145 resulted in the inclusion of gains on repurchases of debt for the three and nine months ended September 30, 2003 and 2002, in investment, interest and other income rather than as an extraordinary item in the financial statements.

Accounting for Costs Associated with Exit and Disposal Activities

In January 2003, the Company adopted SFAS No. 146. This standard requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operation, plant closing, or other exit or disposal activity. This statement is applicable to exit or disposal activities initiated after December 31, 2002.

Accounting for and Disclosure of Guarantees

In January 2003, the Company adopted FIN 45, which elaborates on the disclosures required to be made by a guarantor in its financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The recognition and initial measurement provisions of FIN 45 were applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 were effective for periods ending after December 15, 2002. The adoption of FIN 45 did not have a material impact on the Company’s financial position or results of operations.

Consolidation of Variable Interest Entities

In January 2003, the FASB issued FIN 46, which establishes criteria to identify and assess a company’s interest in variable interest entities and for consolidating those entities. FIN 46 is currently effective for variable interest entities created or obtained after January 2003, and will be effective for all variable interest entities for interim periods beginning after December 15, 2003. The Company believes that the adoption of FIN 46 may require the consolidation of a 50% interest in a joint venture (FireRock, LLC) which develops real estate in Arizona.

3. Segment Information and Other Items

Net sales and operating income (loss) for each reportable segment is presented in the Consolidated Statement of Operations. Operating income (loss) for "Corporate" represents general and administrative expenses not directly attributable to the reportable segments. The amounts reflected in the "Corporate" column also serve to reconcile the total of the reportable segments' amounts to totals in the Company's consolidated financial statements.

The following table presents certain other unaudited financial information by reportable segment (in millions).

	Reportable Segments						
	Forest Products	Real Estate	Racing	Corporate	Consolidated Total Excluding Aluminum	Aluminum	Consolidated Total
Depreciation, depletion and amortization for the three months ended:							
September 30, 2003	$ 5.1	$ 3.6	$ 0.4	$ –	$ 9.1	$ –	$ 9.1
September 30, 2002	5.8	2.5	0.4	0.1	8.8	–	8.8
Depreciation, depletion and amortization for the nine months ended:							
September 30, 2003	15.8	10.8	1.2	0.1	27.9	–	27.9
September 30, 2002	17.6	7.5	1.2	0.3	26.6	9.7 [1]	36.3
Total assets as of:							
September 30, 2003	488.4	361.2	34.7	179.7	1,064.0	– [2]	1,064.0
December 31, 2002	525.3	377.1	36.4	168.5	1,107.3	–	1,107.3

(1) Amounts attributable to the aluminum segment are for the period from January 1, 2002, through February 11, 2002.

(2) As a result of the deconsolidation of Kaiser as of February 11, 2002, the aluminum segment's balance sheet amounts are not included in the consolidated totals.

Other Items

Real Estate

The real estate segment's investment, interest and other income (expense) includes the following (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Equity in earnings (loss) from real estate joint ventures	$ 0.2	$ (0.4)	$ 1.2	$ 2.4

In March 2003, the Company's casino facility at its Palmas del Mar operation in Puerto Rico ceased operations due to the closure of a hotel which was owned and operated by a third party from whom the casino leased adjacent space. The hotel was sold during the three months ended September 30, 2003, and the Company expects that the new owner will not lease space for the casino to the Company. In connection with such determination, the Company recorded a charge to operating costs of $1.4 million to write-down casino-related assets to estimated fair value.

Corporate

Corporate investment, interest and other income (expense) for the nine months ended September 30, 2003, includes $8.0 million of insurance recoveries related to the *OTS* and *FDIC actions* discussed in Note 8.

4. Restricted Cash, Cash Equivalents, Marketable Securities and Other Investments

The following amounts are restricted (in millions):

	September 30, 2003	December 31, 2002
Current assets:		
Restricted cash and cash equivalents	$ 4.5	$ 9.9
Marketable securities, restricted:		
Amounts held in SAR Account	22.2	19.3
Long-term restricted cash, marketable securities and other investments:		
Amounts held in SAR Account	85.5	101.6
Other amounts restricted under the Timber Notes Indenture	2.6	2.6
Other long-term restricted cash	8.7	10.7
Less: Amounts attributable to repurchased Timber Notes held in SAR Account	(51.5)	(51.3)
	45.3	63.6
Total restricted cash, cash equivalents, marketable securities and other investments	$ 72.0	$ 92.8

5. Investment in Kaiser

Kaiser, its principal operating subsidiary, KACC, and 24 of KACC's wholly owned subsidiaries have filed separate voluntary petitions in the Bankruptcy Court for reorganization under Chapter 11 of the Code. The Original Debtors filed petitions on February 12, 2002. Additional subsidiaries of KACC filed petitions in the first quarter of 2003. The Cases are being jointly administered with the Debtors managing their businesses in the ordinary course as debtors-in-possession subject to the control and administration of the Bankruptcy Court.

The necessity for filing the Cases by the Original Debtors was attributable to the liquidity and cash flow problems of Kaiser arising in late 2001 and early 2002. Kaiser was facing significant near-term debt maturities at a time of unusually weak aluminum industry business conditions, depressed aluminum prices and a broad economic slowdown that was further exacerbated by the events of September 11, 2001. In addition, Kaiser had become increasingly burdened by asbestos litigation and growing legacy obligations for retiree medical and pension costs. The confluence of these factors created the prospect of continuing operating losses and negative cash flows, resulting in lower credit ratings and an inability to access the capital markets.

Kaiser has indicated that its objective in the Cases is to achieve the highest possible recoveries for all stakeholders consistent with the Debtors' abilities to pay, and to continue the operation of their businesses. However, there can be no assurance that the Debtors will be able to attain these objectives or achieve a successful reorganization. While valuation of the Debtors' assets and estimation of pre-Filing Date claims at this stage of the Cases are subject to inherent uncertainties, Kaiser has indicated that the Debtors believe that it is likely that their liabilities will be found to exceed the fair value of their assets. The Debtors therefore believe that it is likely that substantially all pre-Filing Date claims will be settled at less than 100% of their face value and the equity of Kaiser's stockholders, including the Company, will be cancelled without consideration.

As provided by the Code, the Original Debtors had the exclusive right to propose a plan of reorganization for 120 days following the initial Filing Date. The Bankruptcy Court has subsequently approved several extensions of the exclusivity period for all Debtors. A motion to extend the exclusivity period through February 29, 2004, was filed by the Debtors in late October 2003, and the Debtors expect the motion to be approved by the Bankruptcy Court. Kaiser has related that additional extensions are likely to be sought. However, no assurance can be given that any future extension requests will be granted by the Bankruptcy Court. If the Debtors fail to file a plan of reorganization during the exclusivity period, or if such plan is not accepted by the requisite number of creditors and equity holders entitled to vote on the plan, other parties in interest in the Cases may be permitted to propose their own plan(s) of reorganization for the Debtors.

In April 2002, Kaiser filed a motion seeking an order of the Bankruptcy Court prohibiting the Company (or MGHI), without first seeking Bankruptcy Court relief, from making any disposition of the Kaiser Shares, including any sale, transfer, or exchange of such stock or treating any of the Kaiser Shares as worthless for federal income tax purposes. Kaiser indicated in its Bankruptcy Court filing that it was concerned that such a transaction could have the effect of depriving Kaiser of the ability to utilize the full value of its net operating losses, foreign tax credits and minimum tax credits. In July 2002, the Company and MGHI agreed with Kaiser that they would not dispose of any of their Kaiser Shares prior to a hearing on the April 2002 motion. The parties also agreed that the Company (or MGHI) may upon 10 days written notice to Kaiser (a) request the Bankruptcy Court to hear the matter at a special hearing or (b) have the matter heard at one of Kaiser's scheduled monthly bankruptcy hearings.

Kaiser's common stock is publicly traded on the OTC Bulletin Board under the trading symbol "KLUCQ." The market value for the 50,000,000 Kaiser Shares, based on the price per share quoted at the close of business on November 7, 2003, was $4.5 million. There can be no assurance that such value would be realized should the Kaiser Shares be sold.

The financial information of Kaiser contained herein has been prepared in accordance with SOP 90-7, and on a going concern basis, which contemplates the realization of assets and the liquidation of liabilities in the ordinary course of business. However, as a result of the Cases, such realization of assets and liquidation of liabilities are subject to a significant number of uncertainties. Since Kaiser's results are no longer consolidated with the Company's results, and the Company believes it is not probable that it will be obligated to fund losses related to its investment in Kaiser under principles of consolidation, any material uncertainties related to Kaiser are not expected to impact the Company's financial results.

The following tables contain summarized financial information of Kaiser (in millions).

	September 30, 2003	December 31, 2002
Current assets	$ 465.1	$ 516.6
Investments in and advances to unconsolidated affiliates	75.9	69.7
Property, plant and equipment, net	970.8	1,009.9
Other assets	534.6	629.2
	$ 2,046.4	$ 2,225.4
Current liabilities	$ 343.5	$ 333.6
Other long-term liabilities	85.3	86.9
Long-term debt	42.3	42.7
Liabilities subject to compromise	2,755.6	2,726.0
Minority interests	123.0	121.8
Stockholders' deficit	(1,303.3)	(1,085.6)
	$ 2,046.4	$ 2,225.4

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net sales	$ 327.1	$ 348.0	$ 1,024.9	$ 1,104.9
Costs and expenses	(402.1)	(412.6)	(1,212.0)	(1,239.9)
Other income (expenses), net	(15.0)	(12.2)	(36.8)	(41.8)
Loss before income taxes, minority interests and discontinued operations	(90.0)	(76.8)	(223.9)	(176.8)
Provision for income taxes	(0.5)	(7.0)	(4.9)	(21.4)
Minority interests	1.9	1.4	5.8	4.3
Loss from continuing operations	(88.6)	(82.4)	(223.0)	(193.9)
Discontinued operations	–	(1.0)	7.9	(4.0)
Net loss	$ (88.6)	$ (83.4)	$ (215.1)	$ (197.9)

6. Short-term Borrowings

The Pacific Lumber Credit Agreement provides for a two-year revolving line of credit expiring on August 13, 2004, with an aggregate commitment of up to $45.0 million (based on the amount of inventories and receivables held by Pacific Lumber). At September 30, 2003, $0.3 million of letters of credit and no borrowings were outstanding under this facility, and unused availability was limited to $24.4 million.

The Scotia LLC Line of Credit allows Scotia LLC to borrow up to one year's interest on the Timber Notes. On June 20, 2003, the Scotia LLC Line of Credit was extended to July 7, 2006. At or near the completion of such extension, Scotia LLC will request that the Scotia LLC Line of Credit be extended for a further period of not less than 364 days. If not extended, Scotia LLC may draw upon the full amount available. The amount drawn would be repayable in 12 semiannual installments on each note payment date (after the payment of certain other items, including the Aggregate Minimum Principal Amortization Amount, as defined, then due), commencing approximately two and one-half years following the date of the draw. At September 30, 2003, Scotia LLC could have borrowed a maximum of $58.5 million under the Scotia LLC Line of Credit, and there was $20.3 million outstanding under the Scotia LLC Line of Credit.

7. Long-term Debt

Long-term debt consists of the following (in millions):

	September 30, 2003	December 31, 2002
6.55% Scotia LLC Timber Notes due July 20, 2028	$ 83.9	$ 103.2
7.11% Scotia LLC Timber Notes due July 20, 2028	243.2	243.2
7.71% Scotia LLC Timber Notes due July 20, 2028	463.3	463.3
7.56% Lakepointe Notes due June 8, 2021	117.8	119.5
7.03% Motel Notes due May 1, 2018	48.8	49.4
6.08% Beltway Notes due November 9, 2024	30.5	30.9
7.12% Palmas Notes due December 20, 2030	30.0	30.0
Other notes and contracts, primarily secured by receivables, buildings, real estate and equipment	24.8	28.7
	1,042.3	1,068.2
Less: current maturities	(30.6)	(30.5)
Timber Notes held in SAR Account	(56.6)	(55.4)
	$ 955.1	$ 982.3

The amount attributable to the Timber Notes held in the SAR Account of $51.5 million as of September 30, 2003, reflected in Note 4 above represents the amortized amount paid to acquire $56.6 million of principal amount of Timber Notes.

In April 2003, $3.4 million of funds from the SAR Account were used to repurchase $4.0 million principal amount of Timber Notes, as permitted under the Indenture, resulting in a gain of $0.4 million (net of unamortized deferred financing costs) on extinguishment of debt, which is included in investment, interest and other income in the accompanying financial statements.

8. Contingencies

Forest Products Operations

Regulatory and environmental matters play a significant role in the Company's forest products business, which is subject to a variety of California and federal laws and regulations, as well as the HCP, dealing with timber harvesting practices, threatened and endangered species and habitat for such species, and air and water quality.

From March 1999 until October 2002, the Company prepared THPs in accordance with the SYP. The SYP was intended to comply with regulations of the California Board of Forestry and Fire Protection requiring timber companies to project timber growth and harvest on their timberlands over a 100-year planning period and to demonstrate that their projected average annual harvest for any decade within a 100-year planning period will not exceed the average annual growth level during the last decade of the 100-year planning period. The forest practice rules allow companies which do not have a sustained yield plan to follow an alternative procedure. As discussed below, on October 31, 2003, the Court hearing the *EPIC-SYP/Permits* and *USWA lawsuits* entered a judgment invalidating the SYP and the California Permits. As a result of this case, Pacific Lumber has since October 2002 been obtaining review and approval of prepared THPs under this alternative procedure and expects to follow this procedure for the foreseeable future.

The HCP and related Federal Permits allow incidental "take" of certain species located on the Company's timberlands which species have been listed by the federal government under the ESA so long as there is no "jeopardy" to the continued existence of such species. The HCP identifies the measures to be instituted in order to minimize and mitigate the anticipated level of take to the greatest extent practicable. The HCP and Federal Permits have a term of 50 years. Since the consummation of the Headwaters Agreement in March 1999, there has been a significant amount of work required in connection with the implementation of the Environmental Plans, and this work could continue for several more years.

Under the CWA, the EPA is required to establish TMDLs in water courses that have been declared to be "water quality impaired." The EPA and the North Coast Water Board are in the process of establishing TMDLs for many northern California rivers and certain of their tributaries, including nine water courses that flow within the Company's timberlands. The Company expects this process to continue into 2010. In December 1999, the EPA issued a report dealing with TMDLs on two of the nine water courses. The agency indicated that the requirements under the HCP would significantly address the sediment issues that resulted in TMDL requirements for these two water courses. The North Coast Water Board has begun the process of establishing the TMDL requirements applicable to two other water courses on the Company's timberlands, with a targeted completion of fall 2004 for these two water courses. The final TMDL requirements applicable to the Company's timberlands may require aquatic protection measures that are different from or in addition to those in the HCP or that result from the prescriptions to be developed pursuant to the watershed analysis process provided for in the HCP.

Effective January 1, 2003, a California statute eliminated a waiver previously granted to, among others, timber companies. This waiver had been in effect for a number of years and waived the requirement under California water quality regulations for timber companies to follow certain waste discharge requirements in connection with their timber harvesting and related operations. The new statute provides, however, that regional water boards such as the North Coast Water Board are authorized to renew the waiver. The North Coast Water Board has renewed the waiver for timber companies through December 31, 2003. Should the North Coast Water Board decide not to extend this or another waiver beyond December 31, 2003, it may thereafter notify a company to follow certain waste discharge requirements in order to conduct harvesting operations on a THP. The waste discharge requirements may include aquatic protection measures that are different from or in addition to those provided for in the THP approved by the CDF. Accordingly, harvesting activities could be delayed and/or adversely affected as these waste discharge requirements are developed and implemented and costs could increase.

In October 2003, California enacted Senate Bill 810, which provides regional water quality control boards with additional authority related to the approval of THPs. Under this law, which will become effective on January 1, 2004, a THP "may not be approved if the appropriate regional water quality control board finds, based on substantial evidence, that the timber operations proposed in the plan will result in a discharge into a watercourse that has been classified as impaired due to sediment...that causes or contributes to a violation of the regional water quality control plan." The Company is uncertain of the operational and financial effects which will ultimately result from Senate Bill 810; however, because substantially all rivers and waterbodies on the Company's timberlands are classified as impaired, implementation of this law could result in delays in obtaining approvals of THPs, increased costs and additional protection measures beyond those contained in the HCP.

The North Coast Water Board has issued orders for the Elk River and Freshwater watersheds requiring Pacific Lumber to submit "Reports of Waste Discharge" to the North Coast Water Board in order to conduct winter harvesting activities in these watersheds. After consideration of these reports, the North Coast Water Board imposed requirements on Pacific Lumber to implement additional mitigation and erosion control practices in these watersheds for the 2002-2003 winter operating period. These additional requirements have somewhat increased operating costs. Reports of Waste Discharge for the 2003-2004 winter operating period have been submitted and the North Coast Water Board imposed requirements similar to those imposed for the 2002 - 2003 winter operating period. In addition, the North Coast Water Board has issued the Elk River Order for the Elk River watershed which is aimed at addressing existing sediment production sites through clean up actions. The North Coast Water Board has also initiated the process which could result in similar orders for the Freshwater and Bear Creek watersheds, and are contemplating similar actions for the Jordon and Stitz Creek watersheds. The Elk River Order, as well as additional orders in the other watersheds (should they be issued), could result in significant costs to Pacific Lumber beginning in 2004 and extending over a number of years. Pacific Lumber has appealed the Elk River Order to the State Water Board, but the appeal is being held in abeyance while the matter is discussed by Pacific Lumber with the North Coast Water Board and its staff.

Lawsuits are pending which seek to prevent the Company from implementing the SYP, implementing certain of the Company's approved THPs, or carrying out certain other operations.

In March 1999, the *EPIC-SYP/Permits lawsuit* was filed. This action alleged, among other things, various violations of the CESA and the California Environmental Quality Act, and challenged, among other things, the validity and legality of the SYP and the California Permits. The plaintiffs sought, among other things, to set aside California's approval of the SYP and the California Permits and injunctive relief to prevent implementation of THPs approved in reliance upon these documents. In March 1999, the *USWA lawsuit* was filed challenging the validity and legality of the SYP. The *EPIC-SYP/Permits* and *USWA lawsuits* were consolidated for trial, which concluded on March 28, 2003. On October 31, 2003, the Court entered a judgment invalidating the SYP and the California Permits due to several deficiencies in agency procedures and the failure of Pacific Lumber to submit a complete and comprehensible SYP. The Court's decision, however, allows for harvesting on THPs which rely on the SYP and were approved prior to July 23, 2003. The short-term effect of the ruling will be to preclude approval, under the SYP, of a small number of THPs which were under review but had not been approved, and which will result in a minor reduction in 2003 harvesting that had been expected from these specific THPs. As a result of this case, Pacific Lumber has since October 2002 been obtaining review and approval of new THPs under a procedure provided for in the forest practice rules that does not depend upon the SYP and the California Permits and expects to follow this procedure for the foreseeable future. In addition, Pacific Lumber is in the process of considering the options available to it in light of this development, including appealing the Court's decision and resubmission of an SYP.

In July 2001, the *Bear Creek lawsuit* was filed. The lawsuit alleges that Pacific Lumber's harvesting and other forestry activities under certain of its approved THPs will result in discharges of pollutants in violation of the CWA. The plaintiff asserts that the CWA requires the defendants to obtain a permit from the North Coast Water Board before beginning timber harvesting and road construction activities, and is seeking to enjoin these activities until such permit has been obtained. The plaintiff also seeks civil penalties of up to $27,500 per day for the defendant's alleged continued violation of the CWA. The Company believes that the requirements under the HCP are adequate to ensure that sediment and pollutants from its harvesting activities will not reach levels harmful to the environment. On October 14, 2003, in connection with certain motions that had been filed, the Court upheld the validity of an EPA regulation which exempts harvesting and other forestry activities from certain discharge requirements. Both state and federal agencies, along with Pacific Lumber and other timber companies, have relied upon this regulation for more than 25 years. However, the Court interpreted the regulation in such a way as to narrow the forestry operations which are exempted, thereby limiting the regulation's applicability. This ruling has widespread implications for the timber industry in the United States. The case is not yet final as the trial has not yet been held, and there are many unresolved issues involving interpretation of the Court's decision and its application to actual operations. Should the decision ultimately become final and held to apply to Pacific Lumber's timber operations, it may have some or all of the following effects: impose additional permitting requirements, delay approvals of THPs, increase harvesting costs, and add water protection measures beyond those contained in the HCP. Nonetheless, due to the historical reliance by timber companies on the regulation, it is not likely that civil penalties will be awarded for operations that occurred prior to the Court's decision. While the impact of a conclusion to this case that upholds the October 14, 2003 ruling may be adverse, the Company does not believe that such an outcome would have a material adverse impact on the Company's consolidated financial condition, results of operations and/or liquidity. Nevertheless, due to the numerous ways in which the Court's interpretation of the regulation could be applied to actual operations, there can be no assurance that this will be the case.

On November 20, 2002, the *HWC lawsuit* was filed seeking to enjoin timber operations in the Elk and Freshwater watersheds of the Company's timberlands until and unless the regional and state water boards imposed on those operations waste discharge requirements that met standards demanded by the plaintiff. In August 2003, this case was dismissed by the Court at the request of the plaintiff.

On February 24, 2003, the recently elected District Attorney of Humboldt County filed the *Humboldt DA action*. The suit was filed under the California unfair competition law and alleges that Pacific Lumber, Scotia LLC and Salmon Creek used certain unfair business practices in connection with completion of the Headwaters Agreement, and that this resulted in the ability to harvest significantly more trees under the Environmental Plans than would have otherwise been the case. The suit seeks a variety of remedies including a civil penalty of $2,500 for each additional tree that has been or will be harvested due to this alleged increase in harvest, as well as restitution and an injunction in respect of the additional timber harvesting allegedly being conducted. A hearing on the Company's motions for sanctions and requested dismissal of the case was held on July 28, 2003, and the Company is awaiting the Court's decision. The Company believes that this suit is without merit; however, there can be no assurance that the Company will prevail or that an adverse outcome would not be material to the Company's consolidated financial position, results of operations and/or liquidity.

In November 2001, Pacific Lumber filed the *THP No. 520 lawsuit* alleging that the State Water Board had no legal authority to impose mitigation measures that were requested by the staff of the North Coast Water Board during the THP review process and rejected by the CDF. When the staff of the North Coast Water Board attempted to impose these mitigation measures in spite of the CDF's decision, Pacific Lumber appealed to the State Water Board, which imposed certain of the requested mitigation measures and rejected others. Pacific Lumber filed the *THP No. 520 lawsuit* challenging the State Water Board's decision, and on January 24, 2003, the Court granted Pacific Lumber's request for an order invalidating the imposition of these additional measures. Other claims included in this action have been dismissed by Pacific Lumber without prejudice to its future rights. On March 25, 2003, the State Water Board appealed this decision. While the Company believes the Court's decision will be sustained, a reversal could result in increased demands by the regional and state water boards and their staffs to impose controls and limitations on timber harvesting on Pacific Lumber's timberlands beyond those provided for by the Environmental Plans or could provide additional regulatory powers to the regional and state water boards and their staffs beyond those provided in Senate Bill 810.

Pacific Lumber, Scotia LLC and certain of their affiliates are the defendants in the *Cook action* and the *Cave action*. On April 4, 2003, the plaintiffs in these actions filed amended complaints and served the defendants with notice of the actions. The *Cook action* alleges, among other things, that defendants' logging practices have contributed to an increase in flooding along Freshwater Creek (which runs through Pacific Lumber's timberlands), resulting in personal injury and damage to the plaintiffs' properties. Plaintiffs further allege that in order to have THPs approved in the affected areas, the defendants engaged in certain unfair business practices. The plaintiffs seek, among other things, compensatory and exemplary damages, injunctive relief, and appointment of a receiver to ensure that the watershed is restored. The *Cave action* contains similar allegations and requests similar relief with respect to the Elk River watershed (a portion of which is contained on Pacific Lumber's timberlands). The Company does not believe the resolution of these actions should result in a material adverse effect on its financial condition, results of operations or liquidity.

OTS Contingency and Related Matters

On December 26, 1995, the OTS initiated the *OTS action* against the Company and others alleging, among other things, misconduct by the Respondents and others with respect to the failure of USAT. The OTS sought damages ranging from $326.6 million to $821.3 million under various theories. On October 17, 2002, the *OTS action* was settled for $0.2 million and with no admission of wrongdoing on the part of the Respondents.

On August 2, 1995, the FDIC filed the *FDIC action*. The original complaint was against Mr. Charles E. Hurwitz (Chairman and Chief Executive Officer of the Company) and alleged damages in excess of $250.0 million based on the allegation that Mr. Hurwitz was a controlling shareholder, *de facto* senior officer and director of USAT, and was involved in certain decisions which contributed to the insolvency of USAT. The *FDIC action* has been dismissed as a result of the settlement of the *OTS action.* This dismissal does not affect the *FDIC counterclaim* or motion for sanctions described in the following paragraph.

On May 31, 2000, the Company, Federated and Mr. Hurwitz filed the *FDIC counterclaim* to the *FDIC action*. The *FDIC counterclaim* states that the FDIC illegally paid the OTS to bring claims against the Company, Federated and Mr. Hurwitz. The plaintiffs are seeking reimbursement of attorneys' fees and damages from the FDIC. As of September 30, 2003, such fees, which have been recorded in the Company's Consolidated Statement of Operations as incurred, were in excess of $40.0 million. On November 8, 2002, the Company, Federated and Mr. Hurwitz filed an amended counterclaim and amended motion for sanctions. The Company, Federated and Mr. Hurwitz are vigorously pursuing the *FDIC counterclaim*.

In September 1997, the Company filed suit against a group of its insurers after unsuccessful negotiations with certain of the insurers regarding coverage, under the terms of certain directors and officers liability policies, of expenses incurred in connection with the *OTS* and *FDIC actions*. The insurers requested arbitration, and as a result the lawsuit was dismissed in April 1998. Following binding arbitration with the primary carrier in October 2002, on February 20, 2003, the arbitration panel determined that the insurer should pay the Company approximately $6.5 million plus interest. The Company and the insurer subsequently agreed to settle this matter for $8.0 million, and such amount is reflected in investment, interest and other income (expense) for the nine months ended September 30, 2003. As the limits of the primary policy were not reached by the arbitration panel's award, the Company does not expect to be able to recover any amounts from the other insurers.

The Company's bylaws provide for indemnification of its officers and directors to the fullest extent permitted by Delaware law. The Company is obligated to advance defense costs to its officers and directors, subject to the individual's obligation to repay such amount if it is ultimately determined that the individual was not entitled to indemnification. In addition, the Company's indemnity obligation can, under certain circumstances, include amounts other than defense costs, including judgments and settlements.

On January 16, 2001, the *Kahn lawsuit* was filed. The plaintiff purports to bring this action as a stockholder of the Company derivatively on behalf of the Company. The lawsuit concerns the *OTS* and *FDIC action*s, and the Company's advancement of fees and expenses on behalf of Federated and certain of the Company's directors in connection with these actions. It alleges that the defendants have breached their fiduciary duties to the Company, and have wasted corporate assets, by allowing the Company to bear all of the costs and expenses of Federated and certain of the Company's directors related to the *OTS* and *FDIC* actions. The plaintiff seeks to require Federated and certain of the Company's directors to reimburse the Company for all costs and expenses incurred by the Company in connection with the *OTS* and *FDIC actions*, and to enjoin the Company from advancing to Federated or certain of the Company's directors any further funds for costs or expenses associated with these actions. The parties to the *Kahn lawsuit* have agreed to an indefinite extension of the defendants' obligations to respond to the plaintiffs' claims. Although it is impossible to assess the ultimate outcome of the *Kahn lawsuit*, the Company believes that the resolution of this matter should not result in a material adverse effect on its consolidated financial position, results of operations or liquidity.

Other Matters

The Company is involved in various other claims, lawsuits and proceedings relating to a wide variety of matters. While uncertainties are inherent in the final outcome of such matters and it is presently impossible to determine the actual costs that ultimately may be incurred, management believes that the resolution of such uncertainties and the incurrence of such costs should not result in a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

9. Stock-Based Compensation Plans

Stock options issued to employees and outside directors are accounted for under the intrinsic value method of accounting as defined by APB Opinion No. 25 and related interpretations. The Company has not changed to the fair value based method of accounting for stock-based employee compensation. The following table illustrates the effect on net income and earnings per share had the Company accounted for its stock options under the fair value method of accounting under SFAS No. 123, as amended by SFAS No. 148 (in millions, except per share information):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net loss, as reported	$ (6.3)	$ (7.4)	$ (24.9)	$ (69.4)
Add: Stock-based employee compensation expenses included in reported net loss, net of related tax effects	–	–	–	–
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards, net of related tax effects	(0.4)	(0.4)	(1.3)	(1.0)
Pro forma net loss	$ (6.7)	$ (7.8)	$ (26.2)	$ (70.4)
Basic and diluted loss per share:				
As reported	$ (0.96)	$ (1.14)	$ (3.81)	$ (10.64)
Pro forma	(1.03)	(1.19)	(4.02)	(10.79)

The fair value of stock options granted were estimated at the grant date using a Black-Scholes option pricing model and the following weighted average assumptions:

	Three and Nine Months Ended September 30,	
	2003	2002
Dividend yield	–	–
Expected volatility	0.38	0.36
Risk-free interest rate	4.92%	5.32%
Expected life (years)	6.63	6.59
Weighted average fair value	$ 10.65	$ 13.65

10. Income Taxes

The Company generated a loss before income taxes of $6.3 million for the third quarter of 2003 and $24.9 million for the nine months ended September 30, 2003; however, the Company has recorded no tax benefit associated with the losses for the periods. Each period, the Company evaluates the appropriate factors in determining the realizability of the deferred tax assets attributable to losses and credits generated in the current period and those being carried forward. These factors are discussed further in Note 12 to the Company's consolidated financial statements included in the Form 10-K. Based on this evaluation, the Company provided valuation allowances with respect to the deferred tax assets attributable to losses and credits generated during the three and nine months ended September 30, 2003. These valuation allowances were in addition to the valuation allowances which were provided in prior years.

11. Per Share Information

Basic earnings per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period, including the weighted average impact of the shares of Common Stock issued and treasury stock acquired during the period from the date of issuance or repurchase. For periods in which the Company has net income, basic earnings per share also includes the dilutive effect of Class A Preferred Stock which is convertible into Common Stock. Diluted earnings per share calculations also include the dilutive effect of common and preferred stock options for periods in which the Company has net income.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Weighted average shares outstanding:				
Common Stock	6,517,691	6,527,671	6,522,435	6,527,671
Effect of dilution:				
Class A Preferred Stock [1]	–	–	–	–
Weighted average number of common and common equivalent shares - Basic	6,517,691	6,527,671	6,522,435	6,527,671
Effect of dilution:				
Stock options [1]	–	–	–	–
Weighted average number of common and common equivalent shares - Diluted	6,517,691	6,527,671	6,522,435	6,527,671

[1] The Class A Preferred Stock and options were not included in the computation of basic or diluted earnings per share because the Company had a loss for the three and nine months ended September 30, 2003 and 2002, respectively.

12. Comprehensive Loss

The following table sets forth comprehensive loss (in millions).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net loss:	$ (6.3)	$ (7.4)	$ (24.9)	$ (69.4)
Other comprehensive income (loss):				
Unrealized gains (losses) on available-for-sale investments	(0.4)	0.4	0.4	(0.2)
Applicable income tax benefit (expense)	–	(0.2)	–	0.1
Total comprehensive loss	$ (6.7)	$ (7.2)	$ (24.5)	$ (69.5)

13. Subsequent Event

In November 2003, Pacific Lumber and Scotia LLC sold approximately 681 acres of timberlands within an area known as the Grizzly Creek grove. Pacific Lumber received $10.0 million in cash, while Scotia LLC received $8.2 million in cash. The Company expects to recognize a gain of approximately $16.8 million in the fourth quarter of 2003 related to this sale.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following should be read in conjunction with the financial statements in Part I, Item 1 of this Report and Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Item 8. "Financial Statements and Supplementary Data" of the Form 10-K. Any capitalized terms used but not defined in this Item are defined in the "Glossary of Defined Terms" contained in Appendix A. Except as otherwise noted, all references to notes represent the Condensed Notes to Consolidated Financial Statements included herein.

This Quarterly Report on Form 10-Q contains statements which constitute "forward-looking statements" within the meaning of the PSLRA. These statements appear in a number of places in this section and in Part II. Item 1. "Legal Proceedings." Such statements can be identified by the use of forward-looking terminology such as "believes," "expects," "may," "estimates," "will," "should," "plans" or "anticipates" or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy. Readers are cautioned that any such forward-looking statements are not guarantees of future performance and involve significant risks and uncertainties, and that actual results may vary materially from the forward-looking statements as a result of various factors. These factors include the effectiveness of management's strategies and decisions, general economic and business conditions, developments in technology, new or modified statutory or regulatory requirements, developments in litigation, and changing prices and market conditions. This Form 10-Q and the Form 10-K identify other factors which could cause differences between such forward-looking statements and actual results. No assurance can be given that these are all of the factors that could cause actual results to vary materially from the forward-looking statements.

Results of Operations

The Company operates in three industries: forest products, through MGI and its wholly owned subsidiaries, principally Pacific Lumber, Scotia LLC and Britt; real estate investment and development, managed through MPC; and racing operations through SHRP, Ltd. MGHI owns 100% of MGI and is a wholly owned subsidiary of the Company. In addition, the Company owns 62% of Kaiser, an integrated aluminum producer. All references to the "Company" include MAXXAM Inc. and its majority and wholly owned subsidiaries (but exclusive of Kaiser and its subsidiaries), unless otherwise indicated or the context indicates otherwise. All references to "Kaiser," "MGHI," "Pacific Lumber," "MPC" and "SHRP, Ltd." refer to the respective companies and their subsidiaries, unless otherwise indicated or the context indicates otherwise.

Deconsolidation of Kaiser

Under generally accepted accounting principles, consolidation is generally required for investments of more than 50% of the outstanding voting stock of an investee, except when control is not held by the majority owner. Under these rules, legal reorganization or bankruptcy represent conditions which can preclude consolidation in instances where control rests with the bankruptcy court, rather than the majority owner. As a result of Kaiser's filing for bankruptcy (as discussed in Note 1), Kaiser's financial results were deconsolidated beginning February 12, 2002, and the Company began reporting its investment in Kaiser using the cost method, under which the investment is reflected as a single amount on the Company's balance sheet of $(516.2) million, and the recording of earnings or losses from Kaiser was discontinued after February 11, 2002. Since Kaiser's results are no longer consolidated and the Company believes that it is not probable that it will be obligated to fund losses related to its investment in Kaiser, any adjustments reflected in Kaiser's financial statements subsequent to February 12, 2002 (relating to the recoverability and classification of recorded asset amounts and classification of liabilities or the effects on existing stockholders' deficit as well as adjustments made to Kaiser's financial information for loss contingencies and other matters) are not expected to affect the Company's financial results.

The following financial information is presented for comparison purposes. The financial information for the nine months ended September 30, 2002, is condensed pro forma financial information which reflects the results of operations of the Company excluding Kaiser (in millions, except share data).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net sales	$ 84.2	$ 73.6	$ 227.3	$ 214.8
Costs and expenses	(75.4)	(68.8)	(214.1)	(206.7)
Operating income	8.8	4.8	13.2	8.1
Other income (expenses), net	3.9	2.9	19.8	18.8
Interest expense and amortization of deferred financing costs	(19.0)	(19.7)	(57.9)	(60.2)
Loss before income taxes	(6.3)	(12.0)	(24.9)	(33.3)
Income tax benefit	–	4.6	–	12.1
Minority interests	–	–	–	0.2
Net loss	$ (6.3)	$ (7.4)	$ (24.9)	$ (21.0)
Basic and diluted loss per share	$ (0.96)	$ (1.14)	$ (3.81)	$ (3.22)

See Notes 1 and 5 for further discussion of Kaiser's reorganization proceedings and other information regarding the Company's investment in Kaiser.

Forest Products Operations

Industry Overview and Selected Operational Data

This section contains statements which constitute "forward-looking statements" within the meaning of the PSLRA. See this section and above for cautionary information with respect to such forward-looking statements.

The Company's forest products operations are conducted by MGI, through Pacific Lumber, Scotia LLC and Britt. The segment's business is somewhat seasonal, and its net sales have been historically higher in the months of April through November than in the months of December through March. Management expects that MGI's revenues and cash flows will continue to be somewhat seasonal. Accordingly, MGI's results for any one quarter are not necessarily indicative of results to be expected for the full year.

Regulatory and environmental matters play a significant role in the Company's forest products operations. See Item 1. "Business—Forest Products Operations—Regulatory and Environmental Factors" of the Form 10-K and Note 8 for a discussion of these matters. Regulatory compliance and litigation have caused and may continue to cause delays in obtaining approvals of THPs and delays in harvesting on THPs once they are approved. This could result in a decline in harvest, an increase in the cost of logging operations, and lower net sales, as well as increased costs related to timber harvest litigation.

As discussed in Note 8, the North Coast Water Board is requiring Pacific Lumber to apply certain waste discharge requirements to approved THPs covering winter harvesting operations in the Freshwater and Elk River watersheds, and the North Coast Water Board could require Pacific Lumber to follow waste discharge requirements before harvesting operations are conducted on THPs in other watersheds. These requirements could cause increased costs and delays in harvesting.

Also discussed in Note 8 is the enactment of Senate Bill 810, which provides regional water quality control boards with additional authority related to the approval of THPs. Implementation of this law could result in delays in obtaining approvals of THPs, increased costs and additional protection water measures beyond those contained in the HCP.

Furthermore, there can be no assurance that certain other pending legal, regulatory and environmental matters or future governmental regulations, legislation or judicial or administrative decisions, adverse weather conditions, or low lumber or log prices, will not have a material adverse effect on the Company's financial position, results of operations or liquidity. See Note 8 for further information regarding regulatory and legislative matters and legal proceedings relating to the Company's forest products operations.

During 2001, comprehensive external and internal reviews were conducted of Pacific Lumber's business operations. These reviews were conducted in an effort to identify ways in which Pacific Lumber could operate on a more efficient and cost effective basis. Based upon the results of these reviews, Pacific Lumber, among other things, closed two of its four sawmills, eliminated certain of its operations, including its soil amendment and concrete block activities, began utilizing more efficient harvesting methods and adopted certain other cost saving measures. Further actions may be taken during the next year as a result of Pacific Lumber's continuing evaluation process, and additional writedowns of certain assets may be required.

The following table presents selected operational and financial information for the three and nine months ended September 30, 2003 and 2002, for the Company's forest products operations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
	(In millions of dollars, except shipments and prices)			
Shipments:				
Lumber: [1]				
Redwood upper grades	7.5	7.4	19.8	20.9
Redwood common grades	53.3	55.9	162.1	173.5
Douglas-fir upper grades	1.3	1.0	2.9	3.7
Douglas-fir common grades	12.9	7.3	32.9	12.9
Other	3.4	–	6.5	–
Total lumber	78.4	71.6	224.2	211.0
Wood chips [2]	18.1	19.2	59.9	51.7
Average sales price:				
Lumber: [3]				
Redwood upper grades	$ 1,215	$ 1,291	$ 1,263	$ 1,327
Redwood common grades	632	559	602	546
Douglas-fir upper grades	1,078	1,456	1,321	1,330
Douglas-fir common grades	366	336	348	336
Wood chips [4]	43	34	45	34
Net sales:				
Lumber, net of discount	$ 48.6	$ 44.5	$ 137.8	$ 130.6
Logs	3.0	3.4	4.9	12.2
Wood chips	0.8	0.6	2.7	1.7
Cogeneration power	2.8	2.5	8.8	7.2
Other	0.9	0.8	2.4	2.3
Total net sales	$ 56.1	$ 51.8	$ 156.6	$ 154.0
Operating income	$ 6.7	$ 5.4	$ 16.0	$ 15.3
Loss before income taxes and minority interests	$ (6.1)	$ (8.2)	$ (22.7)	$ (22.8)

(1) Lumber shipments are expressed in millions of board feet.
(2) Wood chip shipments are expressed in thousands of bone dry units of 2,400 pounds.
(3) Dollars per thousand board feet.
(4) Dollars per bone dry unit.

Net Sales

Net sales for the forest products segment increased for the three months ended September 30, 2003, as compared to the same period of 2002. The $4.1 million increase in revenues from lumber sales was primarily due to higher selling prices for redwood common grade lumber. The improvement in revenues due to the increase in prices was partially offset by an unfavorable shift in the mix of lumber from redwood to Douglas-fir. Net sales for the nine months ended September 30, 2003, increased $2.6 million from the comparable prior year period. A $7.3 million decrease in log sales to third parties partially offset increases in net sales for lumber and other products. Lumber sales for the nine months ended September 30, 2003, increased over the prior year period as a result of variances in prices and volumes similar to those between the 2003 and 2002 third quarters. Power sales increased for the nine months ended September 30, 2003 due to an increase in both volume and prices.

Operating Income

Operating income for the forest products segment increased for the quarter and nine months periods ended September 30, 2003 compared to the prior year periods due to increases in net sales of lumber and lower selling, general and administrative expenses in 2003 due principally to lower litigation costs. These improvements were offset in part by an increase in harvesting costs.

Loss Before Income Taxes and Minority Interests

The forest products segment's loss before income taxes and minority interests decreased for the third quarter of 2003 as compared to the third quarter of 2002, primarily due to the increase in operating income discussed above and lower interest expense. Loss before income taxes and minority interests decreased slightly for the first nine months of 2003 versus the comparable prior year period. In addition to the factors which led to the improvement in operating results discussed above, the segment realized lower interest expense and a gain on the repurchase of Timber Notes. These improvements were substantially offset by lower earnings on cash, cash equivalents and short-term investments.

Real Estate Operations

Industry Overview and Selected Operational Data

The Company, principally through its wholly owned subsidiaries, invests in and develops residential and commercial real estate primarily in Arizona, California, Puerto Rico, and Texas. The following table presents selected operational and financial information for the three and nine months ended September 30, 2003 and 2002, for the Company's real estate operations.

	Three Months Ended September 30, 2003	Three Months Ended September 30, 2002	Nine Months Ended September 30, 2003	Nine Months Ended September 30, 2002
	(In millions of dollars)			
Net sales:				
Real estate:				
Fountain Hills	$ 9.0	$ 1.1	$ 16.0	$ 6.0
Mirada	3.4	–	5.3	0.2
Palmas del Mar	0.7	6.2	5.8	12.3
Other	–	1.0	–	1.4
Total	13.1	8.3	27.1	19.9
Resort, commercial and other:				
Fountain Hills	1.2	1.0	3.0	2.8
Mirada	0.2	–	0.2	–
Palmas del Mar	1.9	2.1	6.3	8.4
Commercial lease properties	3.9	2.2	11.9	6.5
Other	0.1	0.1	0.2	0.2
Total	7.3	5.4	21.6	17.9
Total net sales	$ 20.4	$ 13.7	$ 48.7	$ 37.8
Operating income (loss):				
Fountain Hills	$ 6.8	$ (0.2)	$ 9.3	$ (0.2)
Mirada	1.8	(0.5)	0.7	(1.6)
Palmas del Mar	(5.0)	1.1	(9.5)	(0.3)
Commercial lease properties	1.4	0.8	4.4	2.4
Other	(0.1)	0.7	(0.6)	0.4
Total operating income	$ 4.9	$ 1.9	$ 4.3	$ 0.7
Investment, interest and other income (expense), net:				
Equity in earnings from real estate joint ventures	$ 0.2	$ (0.4)	$ 1.2	$ 2.4
Other	0.5	1.1	1.8	3.5
	$ 0.7	$ 0.7	$ 3.0	$ 5.9
Income (loss) before income taxes and minority interests	$ 0.8	$ (0.5)	$ (7.0)	$ (2.9)

Net Sales

The real estate segment reported increases in net sales for both the third quarter and first nine months of 2003 as compared to the same periods of 2002. The increases were driven primarily by higher real estate acreage and commercial lot sales at Fountain Hills, higher residential lot sales at Mirada, and increases in lease revenues from the segment's commercial lease properties (several of which were acquired in the fourth quarter of 2002). These increases were partially offset by declines in real estate acreage sales at Palmas del Mar.

Operating Income and Income (Loss) Before Income Taxes and Minority Interests

Operating income for the real estate segment improved for the third quarter and first nine months of 2003, largely due to the increases in net sales discussed above. Third quarter and year-to-date 2003 operating results included a $1.4 million charge to recognize the impairment of Palmas del Mar's casino assets related to the closure of a hotel which was owned and operated by a third party from whom the casino leased adjacent space. The segment reported income before income taxes and minority interests for the third quarter of 2003 compared to a loss before income taxes and minority interests for the third quarter of 2002. The quarter-over-quarter improvement resulted from increased operating profits in addition to higher income from the segment's FireRock LLC joint venture. The loss before income taxes and minority interests increased for the first nine months of 2003 versus the same period of a year ago despite improvements in operating income primarily due to lower income from the FireRock LLC joint venture, lower interest income, and higher interest expense associated with the borrowings used to finance the acquisition of commercial lease properties in the fourth quarter of 2002.

Racing Operations

Industry Overview and Selected Operational Data

The Company indirectly owns SHRP, Ltd., a Texas limited partnership, which owns and operates Sam Houston Race Park, a Class 1 horse racing facility in Houston, Texas, and Valley Race Park, a greyhound racing facility located in Harlingen, Texas. Results of operations between periods are generally not comparable due to the timing, varying lengths and types of racing meets held. Historically, Sam Houston Race Park and Valley Race Park have derived a significant amount of their annual net pari-mutuel commissions from live racing and simulcasting. Net pari-mutuel commissions have typically been highest during the first and fourth quarters of the year, the time during which Sam Houston Race Park and Valley Race Park have historically conducted live thoroughbred and greyhound racing, respectively.

The following table presents selected operational and financial information for the three and nine months ended September 30, 2003 and 2002, for the Company's racing operations.

	Three Months Ended September 30, 2003	Three Months Ended September 30, 2002	Nine Months Ended September 30, 2003	Nine Months Ended September 30, 2002
	(In millions of dollars)			
Number of live race days:				
Sam Houston Race Park	43	42	91	94
Valley Race Park	–	–	82	84
Handle:				
Sam Houston Race Park:				
On-track handle	$ 37.1	$ 40.0	$ 103.6	$ 111.7
Off-track handle	19.6	23.4	121.9	128.4
Total	$ 56.7	$ 63.4	$ 225.5	$ 240.1
Valley Race Park:				
On-track handle	$ 4.3	$ 5.0	$ 15.8	$ 17.5
Off-track handle	–	–	3.2	2.9
Total	$ 4.3	$ 5.0	$ 19.0	$ 20.4
Net sales:				
Sam Houston Race Park:				
Net pari-mutuel commissions	$ 4.0	$ 4.3	$ 12.3	$ 13.0
Other revenues	3.0	2.9	6.7	6.6
Total	7.0	7.2	19.0	19.6
Valley Race Park:				
Net pari-mutuel commissions	0.5	0.6	2.2	2.4
Other revenues	0.2	0.3	0.8	1.0
Total	0.7	0.9	3.0	3.4
Total net sales	$ 7.7	$ 8.1	$ 22.0	$ 23.0
Operating income (loss):				
Sam Houston Race Park	$ (0.6)	$ (0.4)	$ (0.9)	$ 0.3
Valley Race Park	(0.1)	(0.1)	(0.4)	(0.1)
Total operating income (loss)	$ (0.7)	$ (0.5)	$ (1.3)	$ 0.2
Income (loss) before income taxes and minority interests	$ (0.4)	$ (0.5)	$ (1.1)	$ 0.2

Net Sales

The racing segment reported lower net sales for the quarter and nine months ended September 30, 2003, from the comparable prior year periods. Both Sam Houston Race Park and Valley Race Park experienced lower average daily attendance for simulcast race days which unfavorably impacted net pari-mutuel commissions and net sales.

Operating Income (Loss) and Income (Loss) Before Income Taxes and Minority Interests

Operating results for the racing segment declined for both the quarter and nine months ended September 30, 2003, primarily due to the decreases in net sales discussed above. In addition, results for the nine months ended September 30, 2003, reflected an increase in selling, general and administrative expenses including costs associated with legislative efforts. The segment's loss before income taxes and minority interests was relatively unchanged for the third quarter of 2003 versus the same quarter of 2002; however, the decline in operating results for the first nine months of 2003 led to a loss before income taxes and minority interests for the 2003 year-to-date period as compared to income before income taxes and minority interests for the first nine months of 2002.

Other Items Not Directly Related to Industry Segments

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
	(In millions of dollars)			
Operating loss	$ (2.1)	$ (2.0)[1]	$ (5.8)	$ (8.1)[1]
Income (loss) before income taxes and minority interest	(0.6)	(2.8)	5.9	(7.8)

(1) Includes $0.3 million and $3.5 million of gains on repurchases of debt for the three and nine month periods, respectively, as required by SFAS. No. 145 (see Note 2). These gains were previously reported as extraordinary items.

The operating losses in the table above represent corporate general and administrative expenses that are not allocated to the Company's industry segments. Results for the third quarter and first nine months of 2002 reflect certain general and administrative expenses incurred as a result of Kaiser's Chapter 11 filing, whereas these expenses were significantly less in the comparable periods of 2003. The income (loss) before income taxes and minority interests include operating losses, investment, interest and other income (expense) and interest expense, including amortization of deferred financing costs, that are not attributable to the Company's industry segments. Included in the results for the first nine months of 2003 is income related to an $8.0 million reimbursement from an insurer for certain costs incurred in connection with the *OTS* and *FDIC actions* (see Note 8).

Financial Condition and Investing and Financing Activities

This section contains statements which constitute "forward-looking statements" within the meaning of the PSLRA. See this section and above for cautionary information with respect to such forward-looking statements.

Overview

The Company conducts its operations primarily through its subsidiaries. Creditors of subsidiaries of the Company have priority with respect to the assets and earnings of such subsidiaries over the claims of the creditors of the Company. Certain of the Company's subsidiaries, principally Pacific Lumber and Scotia LLC, are restricted by their various debt instruments as to the amount of funds that can be paid in the form of dividends or loaned to affiliates. Scotia LLC is highly leveraged and has significant debt service requirements. **"MAXXAM Parent"** is used in this section to refer to the Company on a stand-alone basis without its subsidiaries.

The following table summarizes certain data related to financial condition and to investing and financing activities of the Company and its subsidiaries. As a result of the deconsolidation of Kaiser, the balances at September 30, 2003 and December 31, 2002 exclude amounts attributable to Kaiser. For comparison purposes, such amounts have also been excluded from the selected information related to changes in cash and cash equivalents for the nine months ended September 30, 2002.

	Forest Products							
	Scotia LLC	Pacific Lumber	MGI and Other	Real Estate	Racing	MGHI	MAXXAM Parent	Total
				(in millions of dollars)				
Debt and credit facilities (excluding intercompany notes)								
Short-term borrowings and current maturities of long-term debt:								
September 30, 2003	$ 38.6	$ 0.2	$ –	$ 12.1	$ –	$ –	$ –	$ 50.9
December 31, 2002	16.7	0.3	–	13.5	–	–	–	30.5
Long-term debt, excluding current maturities:								
September 30, 2003	$ 715.6	$ 0.3	$ –	$ 238.6	$ 0.6	$ –	$ –	$ 955.1
December 31, 2002	737.7	0.4	–	244.0	0.2	–	–	982.3
Revolving credit facilities:								
September 30, 2003:								
Facility commitment amounts	$ 58.5	$ 45.0	$ 2.3	$ 14.0	$ –	$ –	$ –	$ 119.8
Borrowings	20.3	–	–	–	–	–	–	20.3
Letters of credit	–	0.3	–	2.4	–	–	–	2.7
Unused and available credit	38.2	24.4	2.3	0.3	–	–	–	65.2
Cash, cash equivalents, marketable securities and other investments								
September 30, 2003:								
Current amounts restricted for debt service	$ 22.2	$ –	$ –	$ 0.2	$ –	$ –	$ –	$ 22.4
Other current amounts	3.4	13.2	14.7	6.6	4.5	–	86.8	129.2
	25.6	13.2	14.7	6.8	4.5	–	86.8	151.6
Long-term amounts restricted for debt service	36.6	–	–	1.4	–	–	–	38.0
Other long-term restricted amounts	–	0.4	2.3	4.6	–	–	–	7.3
	36.6	0.4	2.3	6.0	–	–	–	45.3
	$ 62.2	$ 13.6	$ 17.0	$ 12.8	$ 4.5	$ –	$ 86.8	$ 196.9
December 31, 2002:								
Current amounts restricted for debt service	$ 24.5	$ –	$ –	$ 0.3	$ –	$ –	$ –	$ 24.8
Other current amounts	4.9	21.3	13.6	6.4	5.2	0.3	74.8	126.5
	29.4	21.3	13.6	6.7	5.2	0.3	74.8	151.3
Long-term amounts restricted for debt service	52.9	–	–	1.4	–	–	–	54.3
Other long-term restricted amounts	–	0.4	2.3	6.6	–	–	–	9.3
	52.9	0.4	2.3	8.0	–	–	–	63.6
	$ 82.3	$ 21.7	$ 15.9	$ 14.7	$ 5.2	$ 0.3	$ 74.8	$ 214.9

Table and Notes continued on next page

	Forest Products: Scotia LLC	Forest Products: Pacific Lumber	Forest Products: MGI and Other	Real Estate	Racing	MGHI	MAXXAM Parent	Total
	(in millions of dollars)							
Changes in cash and cash equivalents for the nine month periods								
Capital expenditures:								
September 30, 2003	$ 5.9	$ 3.9	$ 0.9	$ 2.7	$ 1.0	$ –	$ 0.1	$ 14.5
September 30, 2002	4.9	3.8	0.3	3.1	0.5	–	–	12.6
Net proceeds from dispositions of property and investments:								
September 30, 2003	$ 3.2	$ 0.3	$ –	$ –	$ –	$ –	$ –	$ 3.5
September 30, 2002	–	2.0	–	–	–	–	–	2.0
Borrowings (repayments) of debt and credit facilities, net of financing costs:								
September 30, 2003	$ 3.8	$ (0.1)	$ –	$ (6.9)	$ 0.3	$ –	$ –	$ (2.9)
September 30, 2002	(9.4)	(17.8)	(0.5)	0.3	–	(41.4)	–	(68.8)
Dividends and advances received (paid):								
September 30, 2003	$ –	$ 4.6	$ (4.7)	$ 0.5	$ (0.6)	$ –	$ 0.2	$ –
September 30, 2002	(29.4)	29.4	(0.1)	(1.1)	(1.7)	–	2.9	–

MAXXAM Parent and MGHI

The Company may from time to time purchase shares of its Common Stock on national exchanges or in privately negotiated transactions. During the third quarter and first nine months of 2003, the Company purchased an aggregate of 5,000 and 14,600 shares, respectively, of its Common Stock on national exchanges. Subsequent to September 30, 2003, the Company purchased an additional 320,700 shares.

MAXXAM Parent and MGHI own the 50,000,000 Kaiser Shares, representing an approximate 62% interest. As a result of the Cases, the value of Kaiser common stock has declined substantially, and the market value of the Kaiser Shares, based on the price per share quoted at the close of business on November 7, 2003, was $4.5 million. There can be no assurance that such value would be realized should the Kaiser Shares be sold, and it is likely that the Company's ownership interest in Kaiser will be cancelled as a result of a plan of reorganization. See also Notes 1 and 5.

MAXXAM Parent believes that its existing resources will be sufficient to fund its working capital requirements for the next year. With respect to long-term liquidity, MAXXAM Parent believes that its existing cash and cash resources, together with distributions from the real estate and racing segments, should be sufficient to meet its working capital requirements. However, there can be no assurance that this will be the case.

Forest Products Operations

The Scotia LLC Line of Credit allows Scotia LLC to borrow up to one year's interest on the Timber Notes. On June 20, 2003, the Scotia LLC Line of Credit was extended to July 7, 2006. At or near the completion of such extension, Scotia LLC will request that the Scotia LLC Line of Credit be extended for a further period of not less than 364 days. If not extended, Scotia LLC may draw upon the full amount available. The amount drawn would be repayable in 12 semiannual installments on each note payment date (after the payment of certain other items, including the Aggregate Minimum Principal Amortization Amount, as defined, then due), commencing approximately two and one-half years following the date of the draw. At September 30, 2003, Scotia LLC could have borrowed a maximum of $58.5 million under the Scotia LLC Line of Credit, and there was $20.3 million outstanding under the Scotia LLC Line of Credit.

On the note payment date in January 2003, Scotia LLC had $5.6 million set aside in the note payment account to pay the $27.9 million of interest due. Scotia LLC used $22.3 million (in addition to $1.6 million of interest due in respect of Timber Notes held by Scotia LLC) of the funds available under the Scotia LLC Line of Credit to pay the remaining amount of interest due. Scotia LLC repaid $12.1 million of principal on the Timber Notes (an amount equal to Scheduled Amortization) using funds held in the SAR Account.

On the note payment date in July 2003, Scotia LLC used $27.4 million (in addition to $2.0 million due in respect of Timber Notes held by Scotia LLC) of the funds available under the Scotia LLC Line of Credit to pay the entire amount of interest due. Scotia LLC repaid $4.4 million of principal on the Timber Notes (an amount equal to Scheduled Amortization) using funds held in the SAR Account.

With respect to the note payment date in January 2004, Scotia LLC expects to use the funds available under the Scotia LLC Line of Credit to pay a substantial portion of the $27.3 million of interest due (in addition to $2.0 million due in respect of Timber Notes held by the Company). Scotia LLC expects to repay $13.1 million of principal on the Timber Notes (an amount equal to Scheduled Amortization) using funds held in the SAR Account.

In April 2003, $3.4 million of funds from the SAR Account were used to repurchase $4.0 million principal amount of Timber Notes, as permitted under the Timber Notes Indenture, resulting in a gain of $0.4 million (net of unamortized deferred financing costs) on extinguishment of debt.

The Pacific Lumber Credit Agreement provides for a two-year revolving line of credit expiring on August 13, 2004, with an aggregate commitment of up to $45.0 million (based on the amount of inventories and receivables held by Pacific Lumber). At September 30, 2003, $0.3 million of letters of credit and no borrowings were outstanding under the Pacific Lumber Credit Agreement. Unused availability was limited to $24.4 million at September 30, 2003.

Pacific Lumber's cash flows from operations may be adversely affected by diminished availability of logs from Scotia LLC, lower lumber prices, adverse weather conditions, or pending legal, regulatory and environmental matters. See "—Results of Operations—Forest Products Operations" above as well as Note 8 for further discussion of the regulatory, environmental and legal matters affecting harvest levels. Pacific Lumber may require funds available under the Pacific Lumber Credit Agreement and/or additional prepayments by MGI of an intercompany loan in order to meet its working capital and capital expenditure requirements for the next year.

Due to its highly leveraged condition, Scotia LLC is more sensitive than less leveraged companies to factors affecting its operations, including low log prices, governmental regulation and litigation affecting its timber harvesting practices (see "—Results of Operations—Forest Products Operations—Industry Overview and Selected Operational Data" above and Note 8), and general economic conditions. Scotia LLC's cash flows from operations are significantly impacted by harvest volumes and log prices. The Master Purchase Agreement between Scotia LLC and Pacific Lumber contemplates that all sales of logs by Scotia LLC to Pacific Lumber will be at fair market value (based on stumpage prices) for each species and category of timber. The Master Purchase Agreement provides that if the purchase price equals or exceeds the SBE Price and a structuring price set forth in a schedule to the Timber Notes Indenture, the purchase price is deemed to be at fair market value. If the purchase price equals or exceeds the SBE Price, but is less than the structuring price, then Scotia LLC is required to engage an independent forestry consultant to confirm that the purchase price reflects fair market value.

In January 2003, in accordance with the Master Purchase Agreement, Scotia LLC engaged an independent forestry consultant with respect to establishing the purchase prices of logs to be sold to Pacific Lumber in the first half of 2003. The consultant determined that with respect to certain categories of logs, the fair market value was higher than the comparable SBE Price. The prices for redwood logs were on average approximately 20% higher for the first half of 2003 than those for the second half of 2002. There was relatively no price change for Douglas-fir logs.

In June 2003, the State Board of Equalization adopted the new Harvest Value Schedule for the second half of 2003. The prices published in that schedule reflected a 22% increase in the SBE Price for small redwood logs and an 11% increase for small Douglas-fir logs from the prices published for the first half of 2003, and a 7% increase from the price in effect for small redwood logs (i.e., the prices established using the independent forestry consultant) during the first half of 2003.

On August 12, 2003, Standard & Poor's Ratings Services announced that it was lowering its ratings on all classes of the Timber Notes. Ratings on the Class A-1 Timber Notes were lowered from A to BBB+; ratings on the Class A-2 Timber Notes were lowered from A to BBB; and ratings on the Class A-3 Timber Notes were lowered from BBB to BB. Standard & Poor's also indicated that the ratings remain on CreditWatch with negative implications and that the lowered ratings reflect the negative impact that depressed timber prices, lower harvest levels, and higher operating costs have had on Scotia LLC's cash flow available for debt service.

As discussed in Note 13, Pacific Lumber and Scotia LLC received $10.0 million and $8.2 million, respectively, in November 2003 for the sale of timberlands in the Grizzly Creek grove. The proceeds received by Scotia LLC will be used to pay down a portion of the Scotia LLC Line of Credit.

With respect to short-term liquidity, Scotia LLC believes that existing cash available for principal payments from the SAR Account, and funds available under the Scotia LLC Line of Credit, together with cash flows from operations, should provide sufficient funds to meet its working capital, capital expenditures and debt service obligations through 2004; however, there can be no assurance that this will be the case. With respect to long-term liquidity, although the Company expects that cash flows from operations and funds available under the SAR Account and the Scotia LLC Line of Credit should be adequate to meet Scotia LLC's debt service, working capital and capital expenditure requirements, unless log prices continue to improve, there can be no assurance that this will be the case. In addition, cash flows from operations will be adversely affected if harvest levels decline or costs increase as a result of the various regulatory, environmental and litigation matters discussed in "—Results of Operations—Forest Products Operations—Industry Overview and Selected Operational Data" above and Note 8.

With respect to long-term liquidity, although MGI and its subsidiaries expect that their existing cash and cash equivalents, lines of credit and ability to generate cash flows from operations should provide sufficient funds to meet their debt service, working capital and capital expenditure requirements, until such time as Pacific Lumber has adequate cash flows from operations and/or dividends from Scotia LLC, there can be no assurance that this will be the case. Cash flows from operations in the long-term may continue to be adversely affected by the same factors discussed above which are affecting short-term cash flows from operations.

Real Estate Operations

The Arizona Department of Water Resources recently notified the local utility which supplies water to the Company's Fountain Hills project that the demand for water in the utility's service area has exceeded certain statutory requirements. This development could adversely affect, among other things, the Company's ability to develop its remaining acreage in Fountain Hills; however, the Company is still in the process of analyzing what the effects could be. The impacts could include increased costs, delays in development, or the inability to develop the remaining acreage for an indefinite period of time.

In March 2003, the Company's casino facility at its Palmas del Mar operation in Puerto Rico ceased operations due to the closure of a hotel which was owned and operated by a third party from whom the casino leased adjacent space. As discussed further in Note 3, the Company does not expect that it will be able to lease space for its casino operations from the new hotel owner at Palmas, and therefore does not expect cash flows from these operations in the future. Net cash flows from the casino's operations for 2002 were approximately $0.8 million. Furthermore, the Company expects that the new hotel owner will not reopen the hotel until some time in 2004. PDMPI benefitted from the revenues generated as a result of guests of the hotel using PDMPI's golf course and other resort related assets, and the hotel's closure could adversely affect the performance of PDMPI in other ways which are not able to be quantified.

The Company believes that the existing cash and credit facilities of its real estate subsidiaries, excluding PDMPI, are sufficient to fund the working capital and capital expenditure requirements of such subsidiaries for the next year. With respect to the long-term liquidity of such subsidiaries, the Company believes that their ability to generate cash from the sale of their existing real estate, together with their ability to obtain financing and joint venture partners, should provide sufficient funds to meet their working capital and capital expenditure requirements. However, if the Company experiences long-term delays in developing its remaining acreage in Fountain Hills as a result of an inability to obtain adequate water supplies, then cash flows from the subsidiaries involved in this development may be significantly less. PDMPI and its subsidiaries, however, have required advances from MAXXAM Parent during 2002 and prior years to fund their operations, and it is expected that PDMPI will require such advances in the future.

Racing Operations

With respect to short-term and long-term liquidity, SHRP, Ltd.'s management expects that SHRP, Ltd. will generate cash flows from operations.

Kaiser's Operations

As a result of the filing of the Cases, claims against the Debtors for principal and accrued interest on secured and unsecured indebtedness existing on the Filing Date are stayed while the Debtors continue business operations as debtors-in-possession, subject to the control and supervision of the Bankruptcy Court. At this time, it is not possible to predict the effect of the Cases on the businesses of the Debtors. With respect to the Company's interest in Kaiser, the Debtors believe that it is likely that the equity of Kaiser's stockholders will be cancelled without consideration. See Note 5 for further information.

Trends

Real Estate Operations

The Arizona Department of Water Resources recently notified the local utility which supplies water to the Company's Fountain Hills project that the demand for water in the utility's service area has exceeded certain statutory requirements. This development could adversely affect, among other things, the Company's ability to develop its remaining acreage in Fountain Hills; however, the Company is still in the process of analyzing what the effects could be. The impacts could include increased costs, delays in development, or the inability to develop the remaining acreage for an indefinite period of time.

Racing Operations

In July 2003, the Texas Racing Commission approved live race dates for 2004. As a result, Sam Houston Race Park will more than double to 95 the number of dates for its quarter horse meet in 2004. The additional live race dates granted for 2004 are not likely to be granted in 2005 and beyond.

The following table presents the number and type of performance conducted and scheduled from 2002 through 2004 at Sam Houston Race Park.

	Years Ended December 31,		
	2002	**2003**	**2004**
Live Thoroughbred Race Days	84	84	78
Live Quarter Horse Race Days	42	43	95
Simulcast-only Days	238	237	192

As a result of the additional live race dates granted for 2004, management expects that revenues will increase somewhat in 2004 as compared to 2003.

The Texas legislature, which convenes every other year and was in session from January 14, 2003 until June 2, 2003, considered a variety of alternatives to address a projected budget shortfall, including enhancing state revenues through additional forms of gaming such as video lottery terminals at existing horse and dog racing tracks, gaming on Indian reservations, keno, and full casinos. The Texas legislature did not enact any of this legislation. While the Company intends to continue pursuing legislation which would expand the form of gaming available at horse and dog tracks, no assurance can be given that these efforts will be successful.

Critical Accounting Policies

See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" of the Form 10-K for a discussion of the Company's critical accounting policies.

New Accounting Pronouncements

See Note 2 for a discussion of new accounting pronouncements and their potential impact on the Company.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to changes in interest rates primarily under the Scotia LLC Line of Credit and the Pacific Lumber Credit Agreement, as well as certain other debt facilities used to finance real estate development activities. These facilities bear interest at either the prime interest rate or LIBOR plus a specified percentage point spread. The Scotia LLC Line of Credit was established in conjunction with the offering of the Timber Notes. The Company's objective in maintaining its other variable rate borrowings is flexibility in borrowing funds and making repayments without penalties. As of September 30, 2003, there were $35.9 million in borrowings outstanding under all variable rate facilities. Based on the amount of borrowings outstanding under these facilities during the nine months ended September 30, 2003, a 1.0% change in interest rates effective from the beginning of the year would have resulted in an increase or decrease in interest expense for the period of $0.2 million.

None of the Company's other debt is exposed to the risk of higher interest payments due to changes in market interest rates. The Company does not utilize interest rate swaps or similar hedging arrangements.

ITEM 4. DISCLOSURE CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Also, the Company has investments in certain unconsolidated entities. As the Company does not control or manage these entities, its disclosure controls and procedures with respect to such entities are necessarily substantially more limited than those it maintains with respect to its consolidated subsidiaries.

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on the foregoing, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

There have been no significant changes in the Company's internal controls or in other factors that could significantly affect the internal controls subsequent to the date the Company completed its evaluation.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth in Note 8 is incorporated herein by reference.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

a. Exhibits:

* 31.1 Section 302 Certification of Chief Executive Officer

* 31.2 Section 302 Certification of Chief Financial Officer

* 32.1 Section 906 Certification of Chief Executive Officer

* 32.2 Section 906 Certification of Chief Financial Officer

* Included with this filing

b. Reports on Form 8-K:

Since the filing of the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2003, the Company has filed or furnished on the dates indicated the following current reports on Form 8-K:

August 14, 2003 - report under Item 12 related to the Company's 2003 second quarter results.

September 29, 2003 - report under Item 5 related to supplemental statement of decision with respect to the *EPIC-SYP/Permits* and *USWA lawsuits*.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, who have signed this report on behalf of the Registrant and as the principal financial and accounting officers of the Registrant, respectively.

MAXXAM INC.

Date: November 14, 2003

By: /S/ PAUL N. SCHWARTZ
Paul N. Schwartz
President, Chief Financial Officer and Director
(Principal Financial Officer)

Date: November 14, 2003

By: /S/ ELIZABETH D. BRUMLEY
Elizabeth D. Brumley
Controller
(Principal Accounting Officer)

APPENDIX A

Glossary of Defined Terms

APB Opinion No. 25: Accounting Principles Board Opinion 25, "Accounting for Stock Issued to Employees"

APB Opinion No. 30: Accounting Principles Board Opinion 30, "Reporting the Results of Operations - Reporting Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions"

Bankruptcy Court: The United States Bankruptcy Court for the District of Delaware

Bear Creek lawsuit: An action entitled *Environmental Protection Information Association v. Pacific Lumber, Scotia Pacific Company LLC* (No. C01-2821) pending in the U.S. District Court for the Northern District of California

Beltway Notes: Beltway Assets LLC's 6.31% notes due in November 2024

Britt: Britt Lumber Co., Inc., a wholly owned subsidiary of MGI

California Permits: The incidental take permits issued by California pursuant to the HCP

Cases: The Chapter 11 proceedings of the Debtors

Cave action: An action entitled *Steve Cave, et al. v. Gary Clark, et al.* (No. DR0220719) pending in the Superior Court of Humboldt County, California

CDF: California Department of Forestry and Fire Protection

CESA: California Endangered Species Act

Class A Preferred Stock: Class A $.05 Non-Cumulative Participating Convertible Preferred Stock of the Company

Code: The United States Bankruptcy Code

Common Stock: $0.50 par value common stock of the Company

Company: MAXXAM Inc. and its majority and wholly owned subsidiaries, unless otherwise indicated or the context indicates otherwise

Cook action: An action entitled *Alan Cook, et al. v. Gary Clark, et al.* (No. DR020718) pending in the Superior Court of Humboldt County, California

CWA: Federal Clean Water Act

Debtors: Kaiser, KACC and the subsidiaries of KACC which have filed petitions for reorganization

Elk River Order: Clean up and abatement order issued to Pacific Lumber by the North Coast Water Board for the Elk River watershed

Environmental Plans: The HCP and the SYP

EPA: Environmental Protection Agency

EPIC-SYP/Permits lawsuit: An action entitled *Environmental Protection Information Association, Sierra Club v. California Department of Forestry and Fire Protection, California Department of Fish and Game, The Pacific Lumber Company, Scotia Pacific Company LLC, Salmon Creek Corporation, et al.* pending in the Superior Court of Humboldt County, California (No. CV990452)

ESA: The federal Endangered Species Act

FASB: Financial Accounting Standards Board

FDIC: Federal Deposit Insurance Corporation

FDIC action: An action filed by the FDIC on August 2, 1995 entitled *Federal Deposit Insurance Corporation, as manager of the FSLIC Resolution Fund v. Charles E. Hurwitz* (No. H-95-3956) in the U.S. District Court for the Southern District of Texas

Federal Permits: The incidental take permits issued by the federal government pursuant to the HCP

FDIC counterclaim: A counterclaim to the *FDIC action* filed on May 31, 2000, by the Company, Federated and Mr. Hurwitz

Federated: Federated Development Company, a principal stockholder of the Company now known as Giddeon Holdings, Inc.

Filing Date: With respect to any particular Debtor, the date on which such Debtor filed its Case

FIN 45: FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others"

FIN 46: FASB Interpretation No. 46, "Consolidation of Variable Interest Entities"

Form 10-K: The Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission for the fiscal year ended December 31, 2002

Harvest Value Schedule: A schedule setting forth SBE Prices which is published bi-annually by the California State Board of Equalization for purposes of computing yield taxes on timber sales

HCP: The habitat conservation plan covering multiple species approved in March 1999, in connection with the consummation of the Headwaters Agreement

Headwaters Agreement: The September 1996 agreement between Pacific Lumber, Scotia LLC, Salmon Creek, the United States and California which provided the framework for the acquisition by the United States and California of the Headwaters Timberlands

Headwaters Timberlands: Approximately 5,600 acres of Pacific Lumber timberlands consisting of two forest groves commonly referred to as the Headwaters Forest and the Elk Head Springs Forest which were sold to the United States and California in March 1999

Humboldt DA action: A civil suit filed in the Superior Court of Humboldt County, California, by the District Attorney of Humboldt County entitled *The People of the State of California v. Pacific Lumber, Scotia Pacific Holding Company and Salmon Creek Corporation* (No. DR030070)

HWC lawsuit: An action entitled *Humboldt County Watershed Council, et al. v. North Coast Regional Water Quality Control Board, et al.* (No. CV03-0438), naming Pacific Lumber as real party in interest, which had been pending in the Superior Court of Humboldt County, California

KACC: Kaiser Aluminum & Chemical Corporation, Kaiser's principal operating subsidiary

Kahn lawsuit: An action entitled *Alan Russell Kahn v. Federated Development Co., MAXXAM Inc., et. al.* (Civil Action 18623NC) pending in the Delaware Court of Chancery

Kaiser: Kaiser Aluminum Corporation, a subsidiary of the Company engaged in aluminum operations

Kaiser Shares: 50,000,000 shares of the common stock of Kaiser owned by the Company and MGHI

Lakepointe Notes: Lakepointe Assets Holdings LLC and its subsidiaries' 7.56% notes due June 8, 2021

LIBOR: London Inter Bank Offering Rate

Master Purchase Agreement: The agreement between Pacific Lumber and Scotia LLC that governs all purchases of logs by Pacific Lumber from Scotia LLC

MGHI: MAXXAM Group Holdings Inc., a wholly owned subsidiary of the Company

MGI: MAXXAM Group Inc., a wholly owned subsidiary of MGHI

Motel Notes: Motel Assets Holdings LLC and its subsidiaries' 7.03% notes due May 1, 2018

MPC: MAXXAM Property Company, a wholly-owned subsidiary of the Company

North Coast Water Board: North Coast Regional Water Quality Control Board

Original Debtors: Kaiser, KACC and the 15 subsidiaries of KACC that filed petitions for reorganization on February 12, 2002

OTS: The United States Department of Treasury's Office of Thrift Supervision

OTS action: A formal administrative proceeding initiated by the OTS against the Company and others on December 26, 1995

Pacific Lumber: The Pacific Lumber Company, a wholly owned subsidiary of MGI

Pacific Lumber Credit Agreement: The revolving credit agreement between Pacific Lumber and a bank which provides for borrowings of up to $45.0 million

Palmas Notes: The 7.12% notes due December 20, 2030 of Palmas Country Club Inc., an indirect wholly owned subsidiary of the Company

PDMPI: Palmas del Mar Properties, Inc., a wholly owned subsidiary of the Company

Permits: The incidental take permits issued by the United States and California pursuant to the HCP

PSLRA: Private Securities Litigation Reform Act of 1995

Respondents: The Company, Federated, Mr. Charles Hurwitz and others

Salmon Creek: Salmon Creek LLC, a wholly owned subsidiary of Pacific Lumber

SAR Account: Funds held in a reserve account titled the Scheduled Amortization Reserve Account and used to support principal payments on the Timber Notes

SBE Price: The applicable stumpage price for a particular species and size of log, as set forth in the most recent Harvest Value Schedule

Scheduled Amortization: The amount of principal which Scotia LLC must pay through each Timber Note payment date in order to avoid prepayment or deficiency premiums

Scotia LLC: Scotia Pacific Company LLC, a limited liability company wholly owned by Pacific Lumber

Scotia LLC Line of Credit: The agreement between a group of lenders and Scotia LLC pursuant to which Scotia LLC may borrow in order to pay up to one year's interest on the Timber Notes

SFAS No. 123: Statement of Financial Accounting Standards No. 123, "Accounting and Disclosure of Stock-Based Compensation"

SFAS No. 143: Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations"

SFAS No. 145: Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections"

SFAS No. 146: Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities"

SFAS No. 148: Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation"

SFAS No. 150: Statement of Financial Accounting Standards No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity"

SHRP, Ltd.: Sam Houston Race Park, Ltd., a wholly-owned subsidiary of the Company

SOP 90-7: American Institute of Certified Public Accountants Statement of Position No. 90-7, "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code"

State Water Board: California State Water Resources Control Board

SYP: The sustained yield plan approved in March 1999, in connection with the consummation of the Headwaters Agreement

THP: Timber harvesting plan required to be filed with and approved by the CDF prior to the harvesting of timber

THP No. 520 lawsuit: An action entitled *The Pacific Lumber Company, et al. v. California State Water Resources Control Board* (No. DR010860) pending in the Superior Court of Humboldt County, California

Timber Notes: Scotia LLC's 6.55% Series B Class A-1 Timber Collateralized Notes, 7.11% Series B Class A-2 Timber Collateralized Notes and 7.71% Series B Class A-3 Timber Collateralized Notes due July 20, 2028

Timber Notes Indenture: The indenture governing the Timber Notes

TMDLs: Total maximum daily load limits

USAT: United Savings Association of Texas

USWA lawsuit: An action entitled *United Steelworkers of America, AFL-CIO, CLC, and Donald Kegley v. California Department of Forestry and Fire Protection, The Pacific Lumber Company, Scotia Pacific Company LLC and Salmon Creek Corporation* (No. 99CS00626) pending in the Superior Court of Sacramento County, California