Berkshire Hathaway Inc.

1973

ANNUAL REPORT TO THE STOCKHOLDERS
(52 WEEKS ENDED DECEMBER 29, 1973)

Contents

Berkshire Hathaway Inc.

To the Stockholders of
Berkshire Hathaway Inc.:

Our financial results for 1973 were satisfactory, with operating earnings of $11,930,592, producing a return of 17.4% on beginning stockholders' equity. Although operating earnings improved from $11.43 to $12.18 per share, earnings on equity decreased from the 19.8% of 1972. This decline occurred because the gain in earnings was not commensurate with the increase in shareholders' investment. We had forecast in last year's report that such a decline was likely. Unfortunately, our forecast proved to be correct.

Our textile, banking, and most insurance operations had good years, but certain segments of the insurance business turned in poor results. Overall, our insurance business continues to be a most attractive area in which to employ capital.

Management's objective is to achieve a return on capital over the long term which averages somewhat higher than that of American industry generally — while utilizing sound accounting and debt policies. We have achieved this goal in the last few years, and are trying to take those steps which will enable us to maintain this performance in the future. Prospects for 1974 indicate some further decline in rate of return on our enlarged equity base.

Textile Operations

Textile demand remained unusually strong throughout 1973. Our main problems revolved around shortages of fiber, which complicated operations and resulted in something less than full utilization of loom capacity. Prices of some fibers skyrocketed during the year.

Cost of Living Council regulations prevented the pricing of many finished products at levels of some of our competitors. However, profits were reasonably commensurate with our capital investment, although below those that apparently might have been achieved had we been able to price at market levels. The textile business has been highly cyclical and price controls may have served to cut down some of the hills while still leaving us with the inevitable valleys.

Because of the extraordinary price rises in raw materials during 1973, which show signs of continuing in 1974, we have elected to adopt the "lifo" method of inventory pricing. This method more nearly matches current costs against current revenues, and minimizes inventory "profits" included in reported earnings. Further information on this change is included in the footnotes to our financial statements.

Insurance Operations

During 1973, Jack Ringwalt retired as President of National Indemnity Company after an absolutely brilliant record since founding the business in 1940. He was succeeded by Phil Liesche who, fortunately for us, possesses the same underwriting and managerial philosophy that worked so well for Jack.

Our traditional business, specialized auto and general liability lines conducted through National Indemnity Company and National Fire and Marine Insurance Company, had an exceptionally fine underwriting year during 1973. We again experienced a decline in volume. Competition was intense, and we passed up the chance to match rate-cutting by more optimistic underwriters. There currently are faint indications that some of these competitors are learning of the inadequacy of their rates (and also of their loss reserves) which may result in easing of market pressures as the year develops. If so, we may again experience volume increases.

Our reinsurance operation had a somewhat similar year — good underwriting experience, but difficulty in maintaining previous volume levels. This operation, guided by the tireless and well-directed efforts of George Young, has been a major profit producer since its inception in 1969.

Our "home state" insurance companies made excellent progress in Nebraska and Minnesota, with both good growth in volume and acceptable loss ratios. We began operations late in the year in Iowa. To date, our big problem has been Texas. In that state we virtually had to start over during 1973 as the initial management we selected proved incapable of underwriting successfully. The Texas experience has been expensive, and we still have our work cut out for us. Overall, however, the home state operation appears to have a promising potential.

Our specialized urban auto operation, Home and Automobile Insurance Company, experienced very poor underwriting in Chicago during 1973. It would appear that rates are inadequate in our primary Cook County marketing area, although the current energy situation confuses the picture. The question is whether possible lowered accident frequency because of reduced driving will more than offset continuing inflation in medical and repair costs, as well as jury awards. We believe that inflation will hurt us more than reduced driving will help us, but some of our competitors appear to believe otherwise.

Home and Auto expanded into Florida and California during the year, but it is too early to know how these moves will prove out financially.

A contributing factor in our unsatisfactory earnings at Home and Auto during 1973 was an accounting system which was not bringing information to management on a sufficiently timely basis. This situation now is being corrected.

On the investment side of our insurance operation, we made substantial additional commitments in common stocks during 1973. We had significant unrealized depreciation — over $12 million — in our common stock holdings at year-end, as indicated in our financial statements. Nevertheless, we believe that our common stock portfolio at cost represents good value in terms of intrinsic business worth. In spite of the large unrealized loss at year-end, we would expect satisfactory results from the portfolio over the longer term.

Banking Operations

The Illinois National Bank & Trust Co. of Rockford again had a record year in 1973. Average deposits were approximately $130 million, of which approximately 60% were time deposits. Interest rates were increased substantially in the important consumer savings area when regulatory maximums were raised at mid-year.

Despite this mix heavily weighted toward interest bearing deposits, our operating earnings after taxes (including a new Illinois state income tax) were again over 2.1% of average deposits.

We continue to be the largest bank in Rockford. We continue to maintain unusual liquidity. We continue to meet the increasing loan demands of our customers. And we continue to maintain our unusual profitability. This is a direct tribute to the abilities of Gene Abegg, Chairman, who has been running the Bank since it opened its doors in 1931, and Bob Kline, our President.

Merger With Diversified Retailing Company, Inc.

Your Directors have approved the merger of Diversified Retailing Company, Inc. into Berkshire Hathaway Inc. on terms involving issuance of 195,000 shares of Berkshire stock for the 1,000,000 shares of Diversified stock outstanding. Because Diversified and its subsidiaries own 109,551 shares of Berkshire, the net increase in the number of shares of Berkshire outstanding after giving effect to this transaction will not exceed 85,449. Various regulatory approvals must be obtained before this merger can be completed, and proxy material will be submitted to you later this year so that you may vote upon it.

Diversified Retailing Company, Inc., through subsidiaries, operates a chain of popular-priced women's apparel stores and also conducts a reinsurance business. In the opinion of your management, its most important asset is 16% of the stock of Blue Chip Stamps.

Blue Chip Stamps

Our holdings of stock in Blue Chip Stamps at year-end amounted to approximately 19% of that company's outstanding shares. Since year-end, we have increased our holdings so that they now represent approximately 22½%; implementation of the proposed merger with Diversified Retailing Company, Inc. would increase this figure to about 38½%.

Our equity in earnings of Blue Chip Stamps became significant for the first time in 1973, and posed an accounting question as to just what period's earnings should be recognized by Berkshire Hathaway Inc. as applicable to the financial statements covered by this annual report.

Blue Chip's fiscal year ends on the Saturday closest to February 28, or two months after the fiscal year-end of Berkshire Hathaway Inc. Or, viewed, alternatively, their year ends ten months prior to Berkshire Hathaway's. An acceptable accounting choice for us, and one which, if made, would not have required an auditor's disclaimer as to scope, was to recognize in our 1973 income an equity of $632,000 in Blue Chip's earnings for their year ended March 3, 1973 with regard to the fewer shares of Blue Chip we owned during this earlier period. But such an approach seemed at odds with reality, and would have meant a ten month lag each year in the future. Therefore, we chose to reflect as 1973 income our equity of $1,008,000 in Blue Chip's earnings based upon unaudited interim earnings through November as publicly reported by Blue Chip Stamps and with regard to our shareholdings during 1973. Because we made this choice of unaudited but current figures, as opposed to the alternative of audited but far from current figures, Peat, Marwick, Mitchell & Co. were unable to express an opinion on our 1973 earnings attributable to Blue Chip Stamps.

The annual report of Blue Chip Stamps, which will contain financial statements for the year ending March 2, 1974 audited by Price, Waterhouse and Company, will be available in early May. Any shareholder of Berkshire Hathaway Inc. who desires an annual report of Blue Chip Stamps may obtain it at that time by writing Mr. Robert H. Bird, Secretary, Blue Chip Stamps, 5801 South Eastern Avenue, Los Angeles, California 90040.

Blue Chip's trading stamp business has declined drastically over the past year or so, but it has important sources of earning power in its See's Candy Shops subsidiary as well as Wesco Financial Corporation, a 54% owned subsidiary engaged in the savings and loan business. We expect Blue Chip Stamps to achieve satisfactory earnings in future years related to capital employed, although certainly at a much lower level than would have been achieved if the trading stamp business had been maintained at anything close to former levels.

Your Chairman is on the Board of Directors of Blue Chip Stamps, as well as Wesco Financial Corporation, and is Chairman of the Board of See's Candy Shops Incorporated. Operating management of all three entities is in the hands of first-class, able, experienced executives.

Sun Newspapers, Inc.

In the 1969 annual report we commented on the purchase of Sun Newspapers Inc., a group of weekly papers published in the metropolitan Omaha area. Since that time we have not commented on their operations in the text of our annual reports, nor have we consolidated their financial results since the operation, because of the small investment involved, has been "financially insignificant."

During 1973 it was made quite apparent that such insignificance did not extend to publishing quality. On May 7th Sun Newspapers was awarded a Pulitzer Prize for local investigative reporting (the first time in history that a weekly had won in this category) for its special section of March 30, 1972 relating to Boys Town. We reported the extraordinary contrast between decreasing services and mounting wealth that had taken place since Father Flanagan's death in 1948.

In addition to the Pulitzer Prize, the reporting job also won the Public Service Award of Sigma Delta Chi, the national society of professional journalists, as well as seven other national awards.

Our congratulations go to Paul Williams, Editor, and Stan Lipsey, Publisher, as well as the entire editorial staff of Sun Newspapers for their achievement, which vividly illustrated that size need not be equated with significance in publishing.

Warren E. Buffett
Chairman of the Board

March 29, 1974

PEAT, MARWICK, MITCHELL & CO.
CERTIFIED PUBLIC ACCOUNTANTS
KIEWIT PLAZA
OMAHA, NEBRASKA 68131

The Board of Directors and Stockholders
Berkshire Hathaway Inc.:

We have examined the consolidated balance sheets of Berkshire Hathaway Inc. and consolidated subsidiaries as of December 29, 1973 and December 30, 1972, the statements of assets and liabilities of the Berkshire Hathaway Inc. - Insurance Group as of December 31, 1973 and 1972, and the related consolidated statements of earnings and retained earnings and changes in financial position of Berkshire Hathaway Inc. for the 52 weeks ended December 29, 1973 and December 30, 1972 and the statements of income and realized investment gains, paid-in and unassigned surplus and changes in financial position of the Berkshire Hathaway Inc. - Insurance Group for the years ended December 31, 1973 and 1972. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances except as stated in the following paragraph.

Blue Chip Stamps, an investee of Berkshire Hathaway Inc., as described in note 4 to consolidated financial statements, was examined by other auditors for its most recent fiscal year ended March 3, 1973. Unaudited earnings of Blue Chip Stamps for the nine months ended December 1, 1973 was the basis in part for the amount of equity in earnings of Blue Chip Stamps recorded by Berkshire Hathaway Inc. Under the terms of our engagement, we did not examine evidence in support of the unaudited earnings and accordingly do not express an opinion as to the equity of $1,008,000 in earnings of Blue Chip Stamps for 1973.

In our opinion, except for the effect of the matter referred to in the preceding paragraph, the aforementioned consolidated financial statements present fairly the financial position of Berkshire Hathaway Inc. and consolidated subsidiaries at December 29, 1973 and December 30, 1972 and the Berkshire Hathaway Inc. - Insurance Group at December 31, 1973 and 1972 and the results of their operations and changes in their financial position for the respective years then ended in accordance with generally accepted accounting principles which, except for the change (of which we approve) in the method of determining inventory valuations, as described in note 6 to consolidated financial statements, have been applied on a consistent basis, after giving retroactive effect to the change, with which we concur, in the basis of presentation as described in note 1 to consolidated financial statements.

Peat, Marwick, Mitchell & Co.

March 20, 1974

Berkshire Hathaway Inc.

AND

Consolidated Subsidiaries

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 29, 1973 and December 30, 1972

	Dec. 29, 1973	Dec. 30, 1972
ASSETS		
Cash	$ 2,885,645	$ 4,998,225
Investments:		
Bonds (note 2)	74,474,461	88,148,480
Preferred stocks (note 3)	2,298,348	2,942,252
Common stocks of unaffiliated companies (note 3)	49,756,778	17,411,780
Common stock of Blue Chip Stamps (note 4)	13,717,274	11,287,396
Unconsolidated bank subsidiary (note 5)	21,003,034	20,472,590
Other unconsolidated subsidiaries (note 5)	1,333,832	1,258,832
Accounts receivable from customers, agents and others (less allowance for doubtful accounts, 1973 — $332,679; 1972 — $226,530)	14,056,574	12,853,881
Inventories (note 6)	7,136,676	6,827,043
Real estate, equipment, furniture and leasehold improvements, at cost less allowance for depreciation and amortization (note 7)	3,668,005	3,640,249
Deferred insurance premium acquisition costs	5,240,000	5,624,000
Other assets	560,987	645,105
	$196,131,614	$176,109,833
LIABILITIES AND STOCKHOLDERS' EQUITY		
Losses and loss adjustment expenses	$ 61,675,768	$ 60,275,018
Unearned premiums	21,281,980	23,839,397
Funds held under reinsurance treaties	1,318,205	957,845
Agents' and policyholders' deposits	471,728	540,742
Amounts due for purchase of securities	459,609	674,123
Accounts payable and accrued expenses	4,726,609	4,383,758
Income taxes:		
Current	262,357	3,576,109
Deferred	3,297,368	3,214,084
7½% debentures due 1987 (note 8)	598,540	641,300
Notes payable to banks (note 9)	—	9,000,000
8% senior notes due 1993 (note 10)	20,000,000	—
Excess of net assets of consolidated subsidiaries over cost of investment	579,070	579,070
Other liabilities	304,914	133,364
	114,976,148	107,814,810
Stockholders' equity:		
Common stock of $5 par value. Authorized at December 29, 1973, 1,100,000 shares, December 30, 1972, 1,722,983 shares; issued at December 29, 1973, 979,569 shares, December 30, 1972, 1,017,547 shares	4,897,845	5,087,735
Retained earnings (note 10)	76,257,621	64,024,663
	81,155,466	69,112,398
Less, at December 30, 1972, cost of 37,978 shares of common stock in treasury	—	817,375
Total stockholders' equity	81,155,466	68,295,023
Contingencies (notes 12 and 14)		
	$196,131,614	$176,109,833

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

52 weeks ended December 29, 1973 and December 30, 1972

	Dec. 29, 1973	*Dec. 30, 1972*
Income items:		
Insurance premiums earned	$ 52,929,257	$ 59,627,050
Net sales of textile products	33,410,551	27,741,969
Interest and dividend income	7,378,109	6,648,359
Real estate income	287,017	310,951
	94,004,934	94,328,329
Cost and expense items:		
Insurance losses and loss adjustment expenses	32,835,798	36,987,030
Cost of textile products sold	28,305,725	23,655,273
Insurance underwriting expenses	16,774,167	18,355,872
Selling, administrative and other expenses	3,363,223	3,119,518
Interest expense	1,606,313	583,724
	82,885,226	82,701,417
Earnings from insurance underwriting and manufacturing operations before applicable income taxes	11,119,708	11,626,912
Income taxes applicable to operating earnings (note 11)	2,979,016	3,240,861
Earnings before equity in net earnings of other companies and realized investment gains	8,140,692	8,386,051
Equity in net earnings of bank subsidiary (note 5)	2,781,900	2,700,353
Equity in net earnings of Blue Chip Stamps (note 4)	1,008,000	111,168
Earnings before realized investment gains	11,930,592	11,197,572
Realized investment gains, net of related income taxes of $401,699 in 1973 and $430,344 in 1972	929,851	928,586
Net earnings	12,860,443	12,126,158
Retained earnings at beginning of year	64,024,663	51,898,505
Excess of cost over par value of treasury stock retired in 1973	(627,485)	—
Retained earnings at end of year	$ 76,257,621	$ 64,024,663
Earnings per share of common stock, based on 979,569 shares outstanding:		
Earnings before realized investment gains	$12.18	$11.43
Realized investment gains	.95	.95
Net earnings	$13.13	$12.38

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

52 weeks ended December 29, 1973 and December 30, 1972

	Dec. 29, 1973	*Dec. 30, 1972*
Funds provided:		
From operations:		
Net earnings	$ 12,860,443	$ 12,126,158
Charges (credits) to earnings not requiring (providing) funds:		
Equity in undistributed earnings of bank subsidiary	(530,444)	(355,744)
Equity in undistributed earnings of Blue Chip Stamps	(900,000)	—
Accretion of discount on bonds	(481,767)	(538,715)
Depreciation and amortization	519,608	536,358
Increase in unpaid losses and loss expense	1,400,750	7,284,393
Decrease in unearned premiums	(2,557,417)	(1,676,871)
(Increase) decrease in accounts receivable from customers, agents and others	(1,202,693)	1,432,787
Increase in inventories	(309,633)	(796,396)
Decrease in deferred insurance premium acquisition costs	384,000	1,147,656
(Decrease) increase in liability for income taxes	(3,230,468)	2,344,510
Increase (decrease) in accounts payable and accrued expenses	342,851	(446,701)
Other, net	332,500	(426,112)
	(6,232,713)	8,505,165
Funds provided from operations	6,627,730	20,631,323
Proceeds from issuance of long-term debt	20,000,000	—
Decrease in cash	2,112,580	526,862
	$ 28,740,310	$ 21,158,185
Funds used:		
Net purchase (sale) of investments:		
Bonds	(14,155,786)	4,921,043
Preferred stocks	(643,904)	1,959,005
Common stocks of unaffiliated companies	32,344,998	6,515,454
Common stock of Blue Chip Stamps	1,529,878	7,159,171
Investment in unconsolidated subsidiary	75,000	—
	19,150,186	20,554,673
Additions to real estate, equipment, furniture and leasehold improvements	547,364	603,512
Repayment of long-term debt	9,042,760	—
	$ 28,740,310	$ 21,158,185

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 29, 1973 and December 30, 1972

(1) Summary of Significant Accounting Policies and Practices

(a) Basis of Presentation

The accounts of Berkshire Hathaway Inc., the parent Company, are consolidated with the accounts of Bourne Mills of Canada, Ltd., a wholly-owned Canadian textile sales subsidiary, and the accounts of subsidiary insurance companies (The "Insurance Group"), wholly-owned by Berkshire Hathaway Inc. This basis of presentation differs from that used in previous financial statements in which the parent Company's investment in the Insurance Group was carried on the equity basis.

The parent Company's investment in The Illinois National Bank & Trust Co. of Rockford is accounted for on the equity basis.

Immaterial subsidiaries are not consolidated and investments therein are carried at cost.

The accounts of the parent Company and its non-insurance subsidiary are maintained on the basis of a fiscal year ending on the Saturday nearest to December 31, while the accounts of the insurance group are maintained on the basis of the calendar year.

(b) Investment in Securities, Other than Affiliates

Investments in bonds are stated at amortized cost, while investments in preferred and common stocks other than affiliates are shown at cost.

(c) Investment in Blue Chip Stamps

The investment in Blue Chip Stamps ("Blue Chip") is accounted for on the equity basis. Deferred income taxes are provided for with respect to undistributed earnings of Blue Chip under the assumption that such earnings will ultimately be distributed as taxable dividends. Blue Chip determines income on the basis of a fiscal year ending on or about February 28. Berkshire Hathaway Inc. reflects its equity in the earnings of Blue Chip on the basis of that company's twelve months ending November 30.

(d) Insurance Premiums

Insurance premiums are recognized as revenues ratably over the terms of the policies. Unearned premiums are computed on the monthly pro rata basis and are stated after deduction for reinsurance placed with other insurers in the amount of $3,281,480 at December 31, 1973 and $3,691,310 at December 31, 1972. Premium acquisition costs such as commission, premium taxes and certain other underwriting expenses are pursuant to statutory insurance accounting rules charged against income when incurred. However, for financial statement purposes, a portion of such costs are deferred and charged against income as the related premiums are earned.

(e) Reserve for Losses

The insurance group provides a reserve for losses and loss adjustment expenses based upon (1) aggregate case basis estimates for losses reported, in respect to direct premiums written, (2) estimates of unreported losses based upon past experience, (3) estimates received relating to assumed reinsurance, and (4) deduction of amounts for reinsurance placed with reinsurers in the amount of $4,421,537 at December 31, 1973 and $3,324,369 at December 31, 1972.

(f) Catastrophe Reserves

The Insurance Group does not provide a reserve for catastrophe losses. The Committee on Insurance Accounting and Auditing of the American Institute of Certified Public Accountants in co-operation with industry representatives is working toward the development of a definitive statement as to the appropriate accounting for catastrophe losses and resolution may lead to changes in the accounting practices being followed.

(g) Real Estate, Equipment, Furniture and Leasehold Improvements

These items of property (including significant betterments and renewals) are carried at cost depreciated over their useful lives estimated at the date of acquisition. The double declining balance method is used to calculate depreciation of new items of textile properties acquired after 1965; the straight-line method is applied for other items. Maintenance, repairs and renewals of a minor nature are generally charged to operations as incurred.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(h) Inventories

Inventories relate to the textile operation and are stated at cost at December 29, 1973, determined under the last-in, first-out method. This represents a change in accounting method; inventories at the beginning of the year and previously were stated at the lower of cost or market on a first-in, first-out basis. See note 6.

(i) Income Taxes

A consolidated Federal income tax return is filed by the parent Company and its eligible subsidiaries. The liability for current income taxes reflected in the consolidated balance sheets represents the apportioned Federal tax liability of the companies whose accounts are consolidated, plus the foreign tax liability of the consolidated noninsurance subsidiary and plus state or provincial income taxes of the consolidated companies.

A provision for deferred taxes is made in recognition of timing differences created by the manner in which the Insurance Group accounts for certain income and expense items for financial reporting purposes and the accounting treatment of these items for income tax purposes.

Investment tax credits on qualifying property and equipment acquisitions are applied as a reduction of income tax expense in the year realized.

(2) Bonds Deposited with Others

Bonds with amortized cost of $13,932,645 and $16,582,277 at December 31, 1973 and 1972, respectively, were deposited in trust with various regulatory authorities or others in accordance with the terms of certain reinsurance treaties.

(3) Investments in Stocks of Unaffiliated Companies

The market values of preferred stocks and common stocks of unaffiliated companies were as follows:

	Dec. 29, 1973	*Dec. 30, 1972*
Preferred stocks	$ 2,186,960	$ 2,872,980
Common stocks of unaffiliated companies	37,344,241	18,698,164

(4) Investment in Blue Chip Stamps

The carrying value of the investment in Blue Chip Stamps ("Blue Chip") at December 29, 1973, represents the cost, less amortization of the excess of cost over equity in net assets at dates of acquisition, plus equity in undistributed earnings. Deferred taxes of $100,000 at December 29, 1973 have been provided with respect to the equity in undistributed earnings assuming their ultimate distribution as a taxable dividend.

The investment in Blue Chip is summarized as follows:

	Dec. 29, 1973	*Dec. 30, 1972*
Shares owned	989,483	853,754
Percentage of total outstanding shares	19%	17%
Cost represented by:		
Underlying net asset values at dates of acquisition	$ 9,115,779	$ 7,704,246
Excess cost, net of amortization of $795,673, December 29, 1973 and $315,673, December 30, 1972	2,905,822	3,267,477
	12,021,601	10,971,723
Equity in post-acquisition undistributed earnings	1,695,673	315,673
	$13,717,274	$11,287,396

The excess cost over underlying net assets is being amortized over eight years from the beginning of 1972.

The stock of Blue Chip is publicly traded in the over-the-counter market, but there is only limited trading in the public market in this stock. The National Association of Insurance Commissioners Valuation Committee assigned to the stock at December 31, 1973 a valuation of $7.25 per share, and $15.375 per share at December 31, 1972. Accordingly, on these bases, the insurance subsidiaries reported in their Convention statements filed with the various state insurance departments an aggregate "market value" of $7,171,502 at December 31, 1973 and $13,130,968 at December 31, 1972 for the shares of Blue Chip held at those respective dates. The Company believes that while such statutory valuations may be indicative of the value in the public market for a moderate number of shares, they are not necessarily indicative of the fair market value of a substantial block of the shares such as that represented by the Berkshire Hathaway holdings.

Blue Chip, a California corporation, is engaged primarily in the furnishing of a trading stamps service in the States of California, Nevada and Oregon and in the development of incentive and marketing programs for business, and through subsidiaries in the manufacture and sale of candy. Blue Chip, at December 31, 1973 owned approximately 45% of Wesco Financial Cor-

NOTES TO FINANCIAL STATEMENTS, *Continued*

poration ("Wesco"), a savings and loan holding company. Subsequent to December 31, 1973, Blue Chip made a tender offer for additional Wesco shares.

The financial statements of Blue Chip as of March 3, 1973 and for the 52 weeks then ended (audited), and as of December 1, 1973 and for the 52 weeks then ended (unaudited) reflect the following:

BLUE CHIP STAMPS
Consolidated Balance Sheets

($000 omitted)

	Mar. 3, 1973	Dec. 1, 1973 (Unaudited)
ASSETS		
Cash	$ 4,196	$ 2,370
Marketable securities, at cost (market, March 3 — $148,302; December 1 — $105,900)	144,601	117,918
Inventories	13,114	20,666
Other current assets	8,940	9,401
Property, fixtures and equipment, net	10,785	10,579
Unamortized debenture discount	1,347	1,068
Investment in Wesco Financial Corporation	—	16,826
Excess of cost over equity in net assets of subsidiary	16,741	16,422
	$199,724	$195,250
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liability for unredeemed trading stamps	$ 93,351	$ 84,548
Current portion of long-term debt	5,751	7,648
Other current liabilities	13,503	13,860
Note payable to bank, less current portion	23,004	23,004
6¾% subordinated debentures due 1978, less current portion	10,840	8,672
Minority interest in subsidiary	150	147
Stockholders' equity	53,125	57,371
	$199,724	$195,250

BLUE CHIP STAMPS
Consolidated Earnings Summaries

($000 omitted)

	52 weeks ended Mar. 3, 1973	52 weeks ended Dec. 1, 1973 (Unaudited)
Stamp service revenues	$ 88,736	$ 63,760
Total revenues	132,323	111,845
Earnings before securities gains or losses and extraordinary charges	8,108	8,537
Net earnings	7,101	9,021
Earnings per share	1.38	1.75

Blue Chip financial statements for their fiscal year ended March 3, 1973 (and for certain prior years) revealed significant litigation proceedings against the Company. The Company stated with regard to certain of these proceedings that a possible result could be "a materially adverse effect on revenues and earnings and under existing market conditions might have a materially adverse effect on its ability to continue its trading stamp business." Additional proceedings involve substantial contingent liabilities; the accountants' opinion covering the financial statements of Blue Chip Stamps as of March 3, 1973 and for the fiscal year then ended, as well as that for certain preceding years, was given subject to the effect, if any, of the legal proceedings referred to.

(5) Investments in Unconsolidated Subsidiaries

The investment in the unconsolidated bank subsidiary represents approximately 98% of the outstanding stock of The Illinois National Bank & Trust Co. of Rockford. The equity method is used in accounting for this investment. See note 12 regarding divestiture of this investment. Financial statements of The Illinois National Bank & Trust Co. of Rockford and subsidiary are presented elsewhere herein.

The carrying values of $22,336,886 at December 29, 1973 and $21,731,422 at December 30, 1972 for all unconsolidated subsidiaries were approximately $2,500,000 in excess of the parent Company's equity in the net assets as reflected in the financial statements of the subsidiaries at those dates. This excess cost originated prior to November 1, 1970 and is not being amortized since it is considered by management to have continuing value over an indefinite period.

(6) Inventories

A summary of inventories follows:

	Dec. 29, 1973	Dec. 30, 1972
Raw materials and supplies	$ 1,047,827	$ 690,219
Stock in process	1,604,824	1,676,141
Griege and finished cloth	4,484,025	4,460,683
	$ 7,136,676	$ 6,827,043

Inventories at December 30, 1972 were, consistent with prior years, stated at the lower of cost (first-in, first-out) or market. Effective with the year ended December 29, 1973, the Company changed its method of determining inventory valuations to cost determined on a basis of last-in, first-out ("LIFO"). This change was made because management believes the use of LIFO will reduce the effect of inflation on stated earnings; current costs will generally be more nearly matched against current revenues in the statements of income. The change had the effect of reducing inventories at December 29, 1973 by $588,348 and net income by $294,714 ($0.30 per share) for the 52 weeks then ended and is reported in accordance with Opinion No. 20 of the Accounting Principles Board. There is no cumulative effect of the change on prior years, since the December 30, 1972 inventory as previously stated is, under the LIFO method, also the amount of the beginning inventory used in calculating cost of sales for 1973.

(7) Real Estate, Equipment, Furniture and Leasehold Improvements

The composition of plant and equipment is shown below:

December 29, 1973	*Properties of textile operations*	*Properties of insurance group*	*Total*
Land	$ 84,860	$ 83,847	$ 168,707
Buildings	2,364,265	1,251,905	3,616,170
Machinery and equipment	12,361,378	—	12,361,378
Furniture and fixtures and leasehold improvements	593,900	935,745	1,529,645
	15,404,403	2,271,497	17,675,900
Less accumulated depreciation and amortization	13,341,570	666,325	14,007,895
	$ 2,062,833	$ 1,605,172	$ 3,668,005
December 30, 1972			
Land	$ 84,860	$ 83,847	$ 168,707
Buildings	2,344,684	1,172,156	3,516,840
Machinery and equipment	11,869,465	—	11,869,465
Furniture and fixtures and leasehold improvements	660,867	964,793	1,625,660
	14,959,876	2,220,796	17,180,672
Less accumulated depreciation and amortization	12,993,741	546,682	13,540,423
	$ 1,966,135	$ 1,674,114	$ 3,640,249

(8) 7½% Subordinated Debentures

Debentures bear interest at the rate of 7½% payable February 1 and August 1 and will be due on August 1, 1987. The debentures are not secured by any lien and are not convertible; they are subordinated to senior indebtedness which includes indebtedness of the parent Company for money borrowed. The debentures may be redeemed at par at the Company's option. The indenture under which the debentures were issued requires the parent Company to redeem $42,800 principal amount of the debentures, through a sinking fund, on August 1 in each of the years 1974 to and including 1986.

(9) Notes Payable to Banks

The parent Company was liable at December 30, 1972 for $9,000,000 under the terms of a term loan agreement with certain banks. These borrowings were refinanced in March 1973. See note 10.

(10) 8% Senior Notes Due 1993

On March 15, 1973, the parent Company issued at par $20,000,000, 8% Senior Notes due March 1, 1993. Part of the proceeds was used to repay $9,000,000 of outstanding bank notes; the remainder of the proceeds was used for additional capital contributions to the Insurance Group.

The notes call for mandatory annual prepayments of $1,143,000 on March 1 in each of the years from 1979 to 1992, inclusive. Optional prepayments are permitted without premium up to the amount of the required prepayments in each of the years 1979 to 1992; this right is not cumulative. Additionally, the parent Company may also prepay the notes at any time, in full or in part, at a premium of 8% in the twelve months commenced March 1, 1973; the premium declines ratably to par in 1992. The parent Company agreed it will not affect any optional prepayment prior to March 1, 1983 from proceeds of any refunding operation involving the incurring of any indebtedness at an effective annual interest rate of less than 8%.

In the note instruments the parent Company agreed, among other things, as to both the parent Company and restricted subsidiaries, as defined, to limitations as to permissible outstanding funded debt and subordinated funded debt and to a limitation on mortgage debt except as to after-acquired property. Further, the parent Company covenanted that it would not make "restricted payments," which term includes dividends or other equity distributions plus investment in unrestricted subsidiaries (those not bound by the terms of the loan agreement), in excess of stated formula amounts. Retained earnings of approximately $21,000,000 as of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

December 29, 1973 and $13,000,000 as of December 30, 1972 are unrestricted by this provision; the remainder is restricted.

The loan agreement also contains limiting terms relating to sales of the Company's assets, mergers and consolidations, and allows the noteholders to demand prepayment, at par, within 60 days of notice that, during the lifetime of Warren E. Buffett, stock ownership in the parent Company by Warren E. Buffett and the members of his immediate family, including certain trusts and charitable organizations, has decreased to less than 15% of the outstanding capital stock of the parent Company.

(11) Income Taxes

Total income tax expense for 1973 is made up of the following:

	U. S. Federal	*Foreign*	*State and local*	*Total*
Current tax expense:				
On earnings from insurance underwriting and manufacturing operations	$2,781,668	$120,021	$94,043	$2,995,732
On dividends from Blue Chip Stamps	16,000	—	—	16,000
On realized investment gains	401,699	—	—	401,699
Deferred tax expense:				
On equity in undistributed earnings of Blue Chip Stamps	100,000	—	—	100,000
On accreted discount on bonds	170,000	—	—	170,000
Credit for tax effect of reduction in deferred insurance premium acquisition costs	(186,716)	—	—	(186,716)
Total income tax expense	$3,282,651	$120,021	$94,043	$3,496,715

Total income tax expense of $3,496,715 amounted to an effective rate of 21.4% on income before taxes, which is less than the amount of $7,851,436 computed by applying the U. S. Federal income tax rate of 48% to income before taxes. The reasons for this difference for 1973 were as follows:

	Amount	*Percent of pretax income*
Tax expense at statutory rate	$7,851,436	48.0%
Increase (reduction) in income taxes resulting from:		
Tax-exempt interest	(2,304,000)	(14.1)
100% dividend exclusion relating to equity in earnings of Illinois National Bank	(1,335,000)	(8.2)
85% dividends received credit:		
On dividends from unaffiliated companies	(542,000)	(3.3)
On equity in earnings of Blue Chip Stamps	(655,000)	(4.0)
Amortization of excess of cost over net assets of subsidiary and investee (not deductible for tax purposes)	290,000	1.8
Miscellaneous	191,279	1.2
Total income tax expense	$3,496,715	21.4%

Similar factors were operative for 1972 when the effective tax rate was 23.2%.

Consolidated income tax returns of the Company have been examined through 1970 by the Internal Revenue Service and deficiencies have been paid.

(12) "One-Bank Holding Company" Status

The Company is a bank holding company under Federal legislation enacted in 1970. It has filed with the Federal Reserve Board an irrevocable election to divest of its holdings in The Illinois National Bank & Trust Co. of Rockford prior to January 1, 1981. No determination has been made as to how it will effect such divestiture, and so long as the Company controls the bank it is subject to the restrictions imposed upon it by the Bank Holding Company Act.

(13) "Savings and Loan Holding Company" Status

The Company, as a result of its investment in Blue Chip Stamps which in turn beneficially owns a significant interest in a federally insured savings and loan association, is a savings and loan holding company under the Savings and Loan Holding Company Amendments of 1967. As such, the Company is subject to the restrictions and regulatory requirements imposed upon it by the Savings and Loan Holding Company Act.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(14) Proposed Merger

The Company, on March 15, 1974 announced that its Board of Directors had approved for submission to the shareholders a proposal to merge Diversified Retailing Company, Inc. ("Diversified") into Berkshire Hathaway Inc. Diversified is engaged in the retail apparel and reinsurance businesses, additionally, it owns 16.2% of the outstanding shares of Blue Chip Stamps; Warren E. Buffett is the largest stockholder of Diversified. Consummation of the merger is subject to a number of conditions, including the approval of certain regulatory agencies and a favorable two-thirds stockholders' vote on the part of each corporation. Additional shares of the Company's stock are proposed to be issued in the transactions, and if the merger is consummated on the basis proposed, the shares of the Company's stock outstanding will increase by approximately 85,000 shares.

Berkshire Hathaway Inc.

INSURANCE GROUP

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF ASSETS AND LIABILITIES

December 31, 1973 and 1972

ASSETS

	1973	*1972*
Bonds, at amortized cost (note 2)	$ 74,474,461	$ 88,148,480
Investments in stocks of unaffiliated companies, at cost (note 3):		
Preferred stocks	2,298,348	2,942,252
Common stocks	49,756,778	17,411,780
	52,055,126	20,354,032
Investment in Blue Chip Stamps (note 4)	13,717,274	11,287,396
Real estate, furniture and equipment (note 7)	1,605,172	1,674,114
Cash and bank deposits	1,465,359	3,044,367
Agents' balances and premiums in course of collection	6,891,777	6,892,288
Reinsurance recoverable on loss payments	498,924	277,741
Investment income due and accrued	1,409,869	1,629,176
Amounts due from sale of securities	107,765	—
Other assets	373,525	552,855
Deferred acquisition costs	5,240,000	5,624,000
	$157,839,252	$139,484,449

LIABILITIES, CAPITAL STOCK AND SURPLUS

	1973	*1972*
Losses and loss adjustment expenses	$ 61,675,768	$ 60,275,018
Unearned premiums	21,281,980	23,839,397
Funds held under reinsurance treaties	1,318,205	957,845
Contingent commissions	288,332	369,152
Other expenses	149,973	210,833
Taxes, licenses and fees	478,036	567,914
Agents' and policyholders' deposits	471,728	540,742
Federal income taxes:		
Current	442,302	3,141,149
Deferred	3,297,368	3,214,084
Amounts due for purchase of securities	459,609	674,123
Other liabilities	273,633	112,901
	90,136,934	93,903,158
Capital stock and surplus (note C):		
Common stock of National Indemnity Company of $10 par value. At December 31, 1973, authorized 750,000 shares, issued 550,000 shares; at December 31, 1972, authorized 500,000 shares, issued 400,000 shares	5,500,000	4,000,000
Common stock of National Fire & Marine Insurance Company of $100 par value. Authorized 50,000 shares; issued 25,000 shares	2,500,000	2,500,000
Paid-in surplus	20,601,250	9,851,250
Unassigned surplus (note 10)	39,101,068	29,230,041
Total capital stock and surplus	67,702,318	45,581,291
	$157,839,252	$139,484,449

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF INCOME AND REALIZED INVESTMENT GAINS

Years ended December 31, 1973 and 1972

	1973	*1972*
Underwriting income:		
Net premiums written	$ 50,371,841	$ 57,950,178
Decrease in unearned premiums	2,557,416	1,676,872
Premiums earned	52,929,257	59,627,050
Losses and loss expenses incurred	32,835,798	36,987,030
	20,093,459	22,640,020
Underwriting expenses:		
Commissions and brokerage	11,033,458	12,305,064
Salaries and other compensation	2,323,863	2,125,645
Taxes, licenses and fees	1,060,329	1,136,177
Other underwriting expenses	1,972,517	1,641,330
Decrease in deferred acquisition costs	384,000	1,147,656
	16,774,167	18,355,872
Net underwriting gain	3,319,292	4,284,148
Investment income:		
Interest on bonds	5,621,743	5,899,570
Dividends on stock (other than from Blue Chip Stamps)	1,688,024	718,762
Real estate income	287,017	310,951
	7,596,784	6,929,283
Investment expenses	313,894	285,209
Net investment income	7,282,890	6,644,074
Profit from underwriting and investments	10,602,182	10,928,222
Other expense	322,287	222,283
Income before Federal income taxes, equity in earnings of Blue Chip Stamps and realized investment gains	10,279,895	10,705,939
Applicable Federal income taxes (note D)	2,346,719	2,761,347
Income before equity in earnings of Blue Chip Stamps and realized investment gains	7,933,176	7,944,592
Equity in earnings of Blue Chip Stamps (note 4)	1,008,000	111,168
Income before realized investment gains	8,941,176	8,055,760
Realized investment gains, net of Federal income taxes of $401,699 in 1973; $430,344 in 1972	929,851	928,586
Net income	$ 9,871,027	$ 8,984,346

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

STATEMENTS OF PAID-IN AND UNASSIGNED SURPLUS
Years ended December 31, 1973 and 1972

PAID-IN SURPLUS

	1973	*1972*
Beginning of year	$ 9,851,250	$ 7,851,250
Contribution from parent	9,750,000	1,500,000
Excess of proceeds over par value of capital stock issued	1,000,000	500,000
End of year	$ 20,601,250	$ 9,851,250

UNASSIGNED SURPLUS

	1973	*1972*
Beginning of year	$ 29,230,041	$ 21,391,886
Net income	9,871,027	8,984,346
Adjustment in 1972, required as a result of change in accounting method — from reflecting investment in stocks at market to reflecting such investments at cost	—	(1,146,191)
End of year	$ 39,101,068	$ 29,230,041

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF CHANGES IN FINANCIAL POSITION

Years ended December 31, 1973 and 1972

	1973	*1972*
Funds provided:		
From operations:		
Net income	$ 9,871,027	$ 8,984,346
Charges (credits) to income not requiring (providing) funds:		
Equity in undistributed earnings of Blue Chip Stamps	(900,000)	—
Accretion of discount on bonds	(481,767)	(538,715)
Depreciation	128,689	109,296
Increase in unpaid losses and loss expense	1,400,750	7,284,393
Decrease in unearned premiums	(2,557,417)	(1,676,871)
Decrease in deferred acquisition costs	384,000	1,147,656
(Decrease) increase in liability for income taxes	(2,615,563)	2,083,559
Other, net	76,206	(438,181)
	(4,565,102)	7,971,137
Funds provided from operations	5,305,925	16,955,483
Additional capital paid in by shareholders	12,250,000	2,500,000
Decrease in cash	1,579,008	1,518,710
	$ 19,134,933	$ 20,974,193
Funds used:		
Net purchase (sale) of investments:		
Bonds	(14,155,786)	4,921,043
Preferred stocks	(643,904)	1,959,005
Common stocks of unaffiliated companies	32,344,998	6,515,454
Common stock of Blue Chip Stamps	1,529,878	7,159,171
	19,075,186	20,554,673
Purchase of real estate, furniture and equipment	59,747	419,520
	$ 19,134,933	$ 20,974,193

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

NOTES TO FINANCIAL STATEMENTS
December 31, 1973 and 1972

(A) Note References

Numerical note references are to Notes to Consolidated Financial Statements of Berkshire Hathaway Inc. and Consolidated Subsidiaries which include the summary of significant accounting policies and practices.

(B) Basis of Presentation

The financial statements of Berkshire Hathaway Inc. — Insurance Group include the accounts of wholly-owned subsidiaries of Berkshire Hathaway Inc. which are engaged in fire and casualty insurance underwriting. The statements are presented on a combined basis with significant intercompany transactions and balances eliminated, and in accordance with generally accepted accounting principles (GAAP) which differ in some respects from principles prescribed or permitted by insurance regulatory authorities in accordance with which the companies maintain their records.

(C) Stockholders' Equity

The following additional common stock was issued during the two years ended December 31, 1973.

National Indemnity Company, $10 par value common stock:
March 1973—150,000 shares for $11,250,000

National Fire & Marine Insurance Company, $100 par value common stock:
July 1972 — 5,000 shares for $1,000,000

Surplus is restricted for dividend purposes by the insurance departments of the states in which the companies do business.

(D) Federal Income Taxes

Federal income tax expense is made up of the following:

	1973	*1972*
Current Federal income tax expense relating to:		
Earnings before income taxes, equity in earnings of Blue Chip Stamps and realized gains	$2,363,435	$2,816,437
Equity in earnings of Blue Chip Stamps	16,000	—
Realized investment gains	401,699	430,344
Deferred Federal income tax expense (credit) relating to:		
Equity in undistributed earnings of Blue Chip Stamps	100,000	—
Accreted discount on bonds	170,000	494,368
Credit for tax effect of reduction in deferred acquisition costs	(186,716)	(549,458)
	$2,864,418	$3,191,691

Total Federal income tax expense of $2,864,418 for 1973 and $3,191,691 for 1972 amounted to effective rates of 22.5% and 26.2% of income before taxes in those respective years. The tax expense is less than that computed by applying the U. S. Federal income tax rate of 48% to income before taxes; the reasons for the difference were as follows:

	1973		*1972*	
	Amount	*Rate*	*Amount*	*Rate*
Tax expense at statutory rate	$6,113,014	48.0%	$5,844,498	48.0%
Increase (reduction) in income taxes resulting from:				
Tax-exempt interest	(2,304,000)	(18.1)	(2,410,000)	(19.8)
85% dividends received credit relating to:				
Dividends received from unaffiliated companies	(542,000)	(4.3)	(233,000)	(1.9)
Equity in earnings of Blue Chip Stamps	(655,000)	(5.1)	—	—
Miscellaneous	252,404	2.0	(9,807)	(.1)
	$2,864,418	22.5%	$3,191,691	26.2%

Berkshire Hathaway Inc.

BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.
BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS
December 31, 1973 and 1972

ASSETS

	1973	*1972*
Cash and due from banks	$ 26,683,653	$ 22,111,475
Investment securities (note 2):		
United States Government obligations	11,354,830	10,614,548
Obligations of states and political subdivisions	47,712,563	50,162,736
Other securities	3,358,350	7,778,900
Loans (note 3)	66,426,338	59,618,025
Bank premises and equipment, at cost less accumulated depreciation (note 4)	1,116,504	1,360,892
Accrued interest receivable and other assets	1,752,096	1,750,315
	$158,404,334	$153,396,891

LIABILITIES AND STOCKHOLDERS' EQUITY

Demand deposits	$ 55,716,465	$ 55,129,900
Time deposits	81,450,028	77,558,396
Total deposits	137,166,493	132,688,296
Accrued taxes and other liabilities (note 5)	835,154	886,645
Total liabilities	138,001,647	133,574,941
Allowance for possible loan losses (note 6)	1,163,658	1,024,601
Stockholders' equity:		
Common stock, $20 par value. Authorized and issued 250,000 shares	5,000,000	5,000,000
Surplus	5,000,000	5,000,000
Undivided profits	8,238,029	7,796,349
Reserve for contingencies	1,001,000	1,001,000
Total stockholders' equity	19,239,029	18,797,349
	$158,404,334	$153,396,891

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, 1973 and 1972

	1973	*1972*
Operating income:		
Interest and fees on loans	$ 5,316,152	$ 4,134,013
Income on Federal funds sold	236,853	109,905
Interest and dividends on:		
United States Government obligations	632,176	598,308
Obligations of states and political subdivisions	2,795,721	2,677,138
Other securities	342,642	524,229
Trust income	450,529	385,389
Service charges on deposit accounts	129,500	127,258
Other operating income	499,862	411,413
Total operating income	10,403,435	8,967,653
Operating expenses:		
Salaries	1,503,374	1,366,702
Employee benefits (note 7)	262,878	238,618
Interest on deposits	4,295,303	3,418,746
Interest on borrowed money	55,303	3,137
Occupancy expense, net (note 4)	417,739	314,221
Furniture and equipment expense (note 4)	252,709	264,366
Provision for possible loan losses (note 6)	16,100	36,900
Other expense	766,862	644,882
Total operating expenses	7,570,268	6,287,572
Income before income taxes, securities gains and extraordinary item	2,833,167	2,680,081
Applicable income taxes (note 5)	61,136	(354)
Income before securities gains and extraordinary item	2,772,031	2,680,435
Securities gains, net of related taxes of $33,939 in 1973 and $72,351 in 1972	33,477	83,715
Income before extraordinary item	2,805,508	2,764,150
Gain on sale of real estate, net of related taxes of $19,305	42,717	—
Net income	$ 2,848,225	$ 2,764,150
Income per share based on 250,000 shares:		
Income before securities gains and extraordinary item	$11.09	$10.72
Securities gains	.13	.34
Extraordinary item	.17	—
Net income	$11.39	$11.06

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years ended December 31, 1973 and 1972

	Common stock	*Surplus*	*Undivided profits*	*Reserve for contingencies*
Balance, January 1, 1972	$5,000,000	$5,000,000	$7,503,803	$1,001,000
Add:				
Net income	—	—	2,764,150	—
Less:				
Cash dividends — $9.60 per share	—	—	(2,400,000)	—
Transfer to allowance for possible loan losses, net of tax of $66,095 (note 6)	—	—	(71,604)	—
Balance, December 31, 1972	5,000,000	5,000,000	7,796,349	1,001,000
Add:				
Net income	—	—	2,848,225	—
Less:				
Cash dividends — $9.20 per share	—	—	(2,300,000)	—
Transfer to allowance for possible loan losses, net of tax of $4,440 (note 6)	—	—	(106,545)	—
Balance, December 31, 1973	$5,000,000	$5,000,000	$8,238,029	$1,001,000

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION
Years ended December 31, 1973 and 1972

	1973	*1972*
Funds provided:		
Increase (decrease) in:		
Stockholders' equity:		
Net income	$ 2,848,225	$ 2,764,150
Cash dividends	(2,300,000)	(2,400,000)
Other, net	(106,545)	(71,604)
Net change in stockholders' equity	441,680	292,546
Deposits	4,478,197	16,840,043
Other, net	454,209	493,308
Total	$ 5,374,086	$ 17,625,897
Funds used:		
Invested in earning assets:		
Loans	6,825,484	5,503,742
Investment securities	(6,130,441)	7,173,845
Direct lease equipment	—	195,009
	695,043	12,872,596
Additions to bank premises and equipment	53,592	49,186
Increase in cash and due from banks	4,572,178	4,278,789
Other, net	53,273	425,326
	$ 5,374,086	$ 17,625,897

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1973 and 1972

(1) Significant Accounting Policies

The accounting policies of The Illinois National Bank & Trust Co. of Rockford (a subsidiary of Berkshire Hathaway Inc.) and its wholly-owned subsidiary, Brown Building Corporation, conform to generally accepted accounting principles and to general practice within the banking industry. The following is a description of the more significant of the policies:

(a) Consolidation

The consolidated financial statements include those of the Bank and its wholly-owned subsidiary. All significant intercompany transactions are eliminated in consolidation.

(b) Investment Securities

Investment securities are stated at cost, adjusted for amortization of premium.

(c) Installment Loans

Installment loans are generally made on a discount basis. Unearned discount is taken into income over the terms of the respective loans.

(d) Bank Premises and Equipment

Bank premises and equipment are stated at cost less accumulated depreciation based on the estimated useful life of each asset. Depreciation is computed on the straight-line method for building and automobiles, and on an accelerated method for improvements, equipment, and drive-in and parking facilities.

(e) Federal Income Taxes

Taxable income is determined using the cash basis of accounting whereas the accrual method of accounting is used in preparation of financial statements. Deferred taxes are provided in recognition of timing differences.

The Bank and its subsidiary join in the filing of a consolidated Federal income tax return with Berkshire Hathaway Inc., the parent company of the Bank.

(2) Investment Securities

The approximate market value of investment securities at December 31, 1973 and 1972 was $66,930,000 and $72,990,000, respectively.

Investment securities with a book value of $9,530,567 and $10,038,639 at December 31, 1973 and 1972, respectively, were pledged to secure public deposits and for other purposes.

(3) Loans

Loans have been reduced by unearned discount of $2,786,609 and $2,226,579 on December 31, 1973 and 1972, respectively.

(4) Bank Premises and Equipment

Bank premises and equipment are recorded at cost less accumulated depreciation of $1,777,091 and $1,676,936 at December 31, 1973 and 1972, respectively. Depreciation expense totaled $188,552 for 1973 and $210,840 for 1972.

(5) Accrued Taxes and Other Liabilities

Accrued taxes and other liabilities in the accompanying consolidated balance sheets include $139,572 and $137,824 of deferred taxes at December 31, 1973 and 1972, respectively. Such deferred taxes relate principally to timing differences arising from reporting taxable income on the cash basis. In addition, deferred taxes are included in the allowance for possible loan losses. Taxes applicable to net income were as follows:

	1973	*1972*
Tax provision applicable to income before securities gains and extraordinary item	$ 61,136	$ (354)
Tax provision applicable to securities gains	33,939	72,351
Tax provision applicable to gain on sale of real estate	19,305	—
	$114,380	$ 71,997

The components of consolidated income tax expense are as follows:

	1973	*1972*
Taxes currently payable:		
Federal	$ 20,364	$ 73,682
State	92,268	—
	112,632	73,682
Deferred income taxes:		
Federal	(38,208)	(1,685)
State	39,956	—
	1,748	(1,685)
	$114,380	$ 71,997

National banks in Illinois were not subject to state income taxes until 1973. Accordingly, no current or deferred state taxes were provided for 1972.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

The sources of timing differences resulting in deferred income taxes and the tax effect of each were as follows:

	1973	*1972*
Net increase in accrued income taken on cash basis on tax return and on accrual basis for books . . .	$101,402	$ 45,781
Net (increase) decrease in accrued expenses taken on cash basis on tax return and on accrual basis for books	(74,557)	383
Deduction for state taxes taken on the cash basis on tax return and on accrual basis for books	(25,097)	—
Final installment of amortization of unearned discount resulting from accrual conversion	—	(47,849)
	$ 1,748	$ (1,685)

Total tax expense amounted to $114,380 (an effective rate of 4.0%) in 1973, and $71,997 (an effective rate of 2.7%) in 1972, a total less than $1,368,778 and $1,295,255 for 1973 and 1972, respectively, computed by applying the U. S. Federal income tax rate of 48% to income before tax. The reasons for these differences are as follows:

	1973		*1972*	
	Amount	*Percent of pretax income*	*Amount*	*Percent of pretax income*
Tax expense at statutory rate .	$1,368,778	48.0%	$1,295,255	48.0%
Increase (reduction) in taxes resulting from:				
Tax-exempt interest . . .	(1,341,946)	(47.1)	(1,285,026)	(47.6)
State income taxes, net of Federal income tax benefits .	68,756	2.4	—	—
Other — net .	18,792	.7	61,768	2.3
Actual tax expense .	$ 114,380	4.0%	$ 71,997	2.7%

(6) Allowance for Possible Loan Losses

The Bank follows the policy of providing additions to the allowance for possible loan losses in accordance with maximum amounts allowed under applicable Federal tax laws. For financial reporting purposes, the provision charged to operating expenses is based upon the Bank's loan loss experience over the last five years.

Transactions in the allowance for possible loan losses for the years ended December 31, 1973 and 1972 were as follows:

	1973	*1972*
Balance at beginning of year . . .	$1,024,601	$ 854,671
Recoveries on loans previously charged off	29,143	29,259
Additions charged to:		
Operating expenses	16,100	36,900
Undivided profits	106,545	71,604
Deferred income taxes . . .	4,440	66,095
	1,180,829	1,058,529
Less loans charged off	17,171	33,928
Balance at end of year	$1,163,658	$1,024,601

The portion of the allowance which was available to absorb possible loan losses was $734,495 at December 31, 1973 and $706,422 at December 31, 1972.

(7) Pension and Profit-Sharing Plan

The Bank has a noncontributory pension plan and a profit-sharing plan for all officers and employees with two full years of service. The pension contribution for 1973 was $8,406 and $6,409 for 1972. The profit-sharing expense was $136,153 and $125,353 in 1973 and 1972, respectively.

As of January 1, 1973 and January 1, 1972, the market value of the pension trust assets exceeded the actuarial values of the vested benefits of the participants.