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WESCO FINANCIAL CORP **10-K**

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CARD 1 DISCLOSURE INC BETHESDA MD. 20816 FOR 12/31/84

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Legend **A** – *always included - included - if occured or significant* **F** – *frequently included* ■ *special circumstances only*

TENDER OFFER/ACQUISITION REPORTS	13D	13 G	14D-1	14D-9	13E-3	13E-4
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WESCO FINANCIAL CORPORATION
LETTER TO SHAREHOLDERS

To Our Shareholders:

Consolidated "normal" operating income (i.e., before all unusual operating income and all net gains from sales of securities) for the calendar year 1984 increased to $10,060,000 ($1.42 per share) from $8,507,000 ($1.20 per share) in the previous year.

Consolidated net income (i.e., after unusual operating income and all net gains from sales of securities), increased to $23,656,000 ($3.32 per share) from $10,553,000 ($1.48 per share) in the previous year.

Despite the high numbers reported, 1984 was a so-so year in terms of real gain in strength. While "normal" net operating income increased satisfactorily, total net income was swollen in a major way only because of an unusual item of operating income and the cashing in of some unrealized appreciation in marketable securities which had occurred in earlier years.

Wesco has two major subsidiaries, Mutual Savings, in Pasadena, and Precision Steel, headquartered in Chicago and engaged in the steel warehousing and specialty metal products businesses. Consolidated net income for the two years just ended breaks down as follows (in 000s except for per-share amounts)(1):

	"Normal" Net Operating Income of Mutual Savings	"Normal" Net Operating Income of Precision Steel Businesses	All Other "Normal" Net Operating Income(2)	Gain from Unrealized Appreciation in Forward Commitment of Mutual Savings to Buy GNMA Certificates	Net Gains on Sales of Securities(3)	Wesco Consolidated Net Income
December 31, 1984 .	$3,476	$2,034	$4,550	$458	$13,138	$23,656
Per Wesco share . .	.49	.29	.64	.06	1.84	3.32
December 31, 1983 .	3,046	1,622	3,839	—	2,046	10,553
Per Wesco share . .	.43	.23	.54	—	.28	1.48

(1) All figures are net of income taxes.

(2) After deduction of interest and other corporate expenses. Income was from ownership of the Mutual Savings' headquarters office building, primarily leased to outside tenants, and interest and dividend income from cash equivalents and marketable securities owned outside the savings and loan subsidiary.

(3) Includes $1,080,000 ($.15 per share), which, under different accounting treatment, might have been both (1) shifted to a different income category and (2) increased by $1,765,000 ($.25 per share). See "Unusual Income and Certain Accounting Quirks in 1984 Reporting" below.

The foregoing breakdown (of the same aggregate earnings) differs somewhat from that used in audited financial statements, which follow standard accounting convention as interpreted from time to time by Wesco's outside auditor. The supplementary breakdown of earnings is furnished because it is considered useful to shareholders.

Much of this letter is a word-for-word repeat of last year's letter with updated numbers. The repetition of wording occurs because it is believed (1) that the duplicated material remains correct and is worth repeating, and (2) that in Wesco's case any time and money required to change wording would be better spent elsewhere.

Parsimony, however, does not wholly predominate. So much kidding occurred concerning the 1960s automobiles in the old photograph of the Mutual Savings' building, which was used in last year's annual report to avoid incurring the cost of a new photograph, that the purse has been opened a little. Shareholders comparing the new photograph (on the inside front cover of this report) with the old will note that the trees have grown a lot in the intervening years. Fortunately, so has the value of the building. See the last section of this letter. The building, which works very well and attracts high quality tenants regarded as friends, is a constant reminder of the good sense of Louis R. Vincenti and Richard D. Aston, the Wesco executives responsible for its creation.

Mutual Savings

Mutual Savings' "normal" net operating income of $3,476,000 in 1984, represented an increase of 14.1% from the $3,046,000 figure the previous year. In both years such "normal" net operating income, while economically real and probably of at least average quality as reported savings and loan industry incomes go, was below the top quality possible because such earnings came entirely or partly from income tax savings obtained through inclusion of Mutual Savings in the consolidated income tax return of a parent corporation. Earnings so derived from income tax savings are not of the top quality possible because they can be impaired by future changes in tax laws and have less cushion in reserve against future adversity than earnings from ordinary operating income on which income taxes have been paid in full in cash at the highest corporate rate and are recoverable from the I.R.S. in the event of future operating losses.

Separate balance sheets of Mutual Savings at yearend 1983 and 1984 are set forth at the end of this annual report. They show (1) total savings accounts rising to $228 million from $203 million the year before, (2) a very high ratio of shareholders' equity to savings account liabilities (probably the highest for any mature U.S. savings and loan association), (3) a substantial portion of savings account liabilities offset by cash equivalents and marketable securities, and (4) a loan portfolio (mostly real estate mortgages) of about $95 million at the end of 1984, down 11% from the $107 million at the end of 1983. The loan portfolio at the end of 1984 bore a fixed average interest rate of only 7.63%, probably the lowest for any U.S. savings and loan association and far below the average interest rate which now must be paid to hold savings accounts.

The capital-rich, mortgage-loan-interest-rate-poor position of Mutual Savings came from (1) success many years ago as a construction lender at above-average interest rates, plus (2) sale in 1980 by Mutual Savings of all branch offices (except for one satellite office in a major shopping center across the street from the Pasadena headquarters) under terms where only the lowest-yielding mortgage loans from its large portfolio were retained, plus (3) drastic curtailment by Mutual Savings of mortgage lending following the sale of its branch offices, plus (4) profits in every recent year, no matter how high interest rates went.

Mutual Savings has remained profitable because the adverse effects from its old low-yielding, fixed-rate mortgage loan portfolio are more than offset by favorable effects from its large shareholders' equity and a tax-equivalent yield on its marketable securities (utility preferred stocks, tax-exempt bonds and common stocks) considerably higher than that prevailing on the mortgage loan portfolio of a typical savings and loan association. The old low-yielding, fixed-rate mortgage loan portfolio has shrunk from pay-backs at 9.8% per year over the last three years, and the shrinkage is expected to continue at about the same rate. With portfolio shrinkage, loan credit quality problems have been reduced to a meaningless trace, because the old mortgages have large real estate equities supporting secured credit extended. And the foreclosed property on hand (mostly 22 vacant, largely oceanfront, acres in Santa Barbara) over a long holding period has plainly become worth considerably more than its $2 million balance sheet carrying cost.

It should be noted, however, that Mutual Savings' total mortgage loan portfolio did not, in substance as distinguished from accounting form, decrease in 1984 by the 11% mentioned above, determined by comparing audited year end balance sheet totals for loans. Mutual Savings has agreed to buy in 1986 U.S. Government guaranteed mortgage equivalents (GNMA certificates) at a price of about $19 million and has pre-funded this forward commitment by buying U.S. Treasury Notes maturing near the time the certificates will be purchased. After taking into account this forward commitment to purchase GNMA certificates, Mutual Savings' total mortgage loan portfolio has, in substance, *increased* by about 7% in 1984.

The 1984 increase in substance of mortgages owned reflects Mutual Savings' intention to keep at least 60% of assets in mortgages or mortgage equivalents, exactly as the Federal Home Loan Bank Board wisely exhorts the savings and loan industry to do if it expects to remain under a regulatory system separate from that of banks. And as a result of anticipated steady shrinkage through repayment of remaining old 7.63% mortgages, combined with purchases of new mortgages or mortgage equivalents bearing much higher interest rates, Mutual Savings expects in due course significantly to raise the average rate of interest on the entire mortgage loan portfolio, thus improving earnings so long as interest rates on savings accounts do not greatly increase. The GNMA certificates purchased for 1986 delivery at a price of about $19 million are expected to yield about 15% on such price, getting under way the process of "blending" the mortgage loan portfolio yield to a higher average level.

Mutual Savings has adapted in its own way to the dramatic changes which have occurred in recent years in interest rates and the regulatory structure of the banking and savings and loan industries. At Mutual Savings, as well as the rest of the savings and loan industry, the standard practice used to be to borrow short from savers while lending long on fixed-rate mortgages, to have high financial leverage for shareholders' equity and to grant mortgagors easy prepayment terms. The practice was profitable for decades but always involved something like a "hurricane risk," and the equivalent of a hurricane came in 1981-82 as interest rates rose to unprecedented levels and caused widespread losses. Results were good for shareholders before 1981-82 only because interest rates were stable or rose slowly as mortgage-loan portfolios steadily and rapidly expanded under a regulatory structure which both fostered growth and protected operating margins by requiring that on all insured savings accounts fixed rates be paid that were slightly higher than the low rates specified for banks. Thus a small deposit-attracting rate advantage over banks was given to savings and loan associations, while competitive pressure was dampened for both types of institution.

Although interest rates have subsided from the 1981-82 peak, the low and slowly changing interest rates of former years are plainly gone with the wind, as are the former government-decreed limits on interest rate competition for savings accounts and the favoritism for savings and loan associations over banks. But an agency of the U.S. Government (FSLIC) continues to insure savings accounts in the savings and loan industry, just as it did before. The result may well be bolder and bolder conduct by many savings and loan associations. A sort of Gresham's law ("bad loan practice drives out good") may take effect for fully competitive but deposit-insured institutions, through increased copying by cautious institutions of whatever apparent-high-yield loan and investment strategies seem to allow competitors to bid away their savings accounts and yet report substantial earnings. If so, if "bold conduct drives out conservative conduct," there eventually could be widespread insolvencies caused by bold credit extensions come to grief.

And if serious credit-quality troubles come to the savings and loan industry, they will merely add to troubles from the borrowed-short, lent-long-at-fixed-rates problem, which is far from completely removed, and which destroys shareholder wealth at startling speed whenever interest rates are rising rapidly, even when the credit quality of mortgagors or other borrowers is excellent.

The Federal Home Loan Bank Board, under its current Chairman Edwin R. Gray, shares Wesco's concerns. Wesco approves its attempts by regulation and by "jaw-boning" to limit follies to come from (1) sharing the U.S. Government's credit with optimistic new entrants to the savings and loan business, often coming from the real estate development and stock brokerage businesses, given ample scope to venture under widened investment authority, and (2) high financial leverage throughout the savings and loan industry, combined with continuing maturity mismatch of fixed rate assets and liabilities. Logic and history would suggest that Mr. Gray is right to pull on the reins, but this is an unpopular task since many powerful activity-cravers feel the bit and create political heat in opposition to even limited (and almost surely inadequate) financial discipline which would protect the federal deposit-insurance system by demanding a significant margin-of-safety factor in financial institutions, just as in bridges. Wesco is not optimistic either that the present rules of the savings and loan game will stand the test of time or that drastic changes in the rules will occur until huge future trouble comes, sooner or later.

Developing a short-term operating plan for Mutual Savings which would sharply increase its reported earnings next year would be a near-absolute cinch. For instance, savings accounts could be expanded greatly by paying a high rate of interest on "jumbo" deposits in $100,000 multiples, and proceeds plus cash equivalents on hand could be placed in long-term mortgages at a substantial current interest spread while, in addition, some origination fees could be "front-ended" into income. However, taking long-term risks into account, it is much harder to find a sound operating plan. Money is the ultimate fungible commodity. In the new order of things, an association is not only in a tough, competitive, commodity-type business on the lending side but also finds that, with decontrol of government-insured rates paid savers, every competitive association has virtually unlimited credit to fund increased lending, by paying premiums over interest rates generally prevailing on savings accounts. Under such conditions, when all risks are considered, including those created by that portion of competitors motivated primarily by short-term effects, it is quite naturally difficult to earn over a long period an attractive return on shareholders' equity. How could it be otherwise?

A few years ago, about the time Mutual Savings reacted to new conditions by curtailing lending and financial leverage, most other associations decided instead to keep lending aggressively but under new adjustable-rate mortgages under which some portion (but far from all) of the interest-rate-fluctuation risk is shifted to the homeowner.

Despite widespread use of these new adjustable-rate mortgages, savings and loan industry earnings remain dependent to a material extent, as they always were, on an interest rate spread attributable to: (1) borrowing short while lending long, and/or (2) making loans which can be priced high enough to provide a profit only because they involve a very material credit risk, compared to the risk of owning government-backed securities of comparable maturity.

Under present conditions of strong competition from bold competitors accompanied by high interest-rate-fluctuation risk, the result tends to be that each year of reported attractive earnings in the savings and loan industry occurs only in the absence of two now much more likely events: (1) sharply rising interest rates, and (2) widespread credit losses. Thus, each good year reported is a lot like the year when a Texas hurricane insurer reports satisfactory earnings because there have been no hurricanes. Mutual Savings has a considerable share of this uncomfortable position and will continue to have it. It has not yet developed a long-term operating strategy with which it is satisfied, and it continues to seek one. Just as Mutual Savings has been idiosyncratic in the past as it sold branch offices in 1980 (a practice since adopted to some extent by other savings and loan associations and major banks), it will probably be idiosyncratic in the future. It will seek some non-standard way of rendering socially constructive service while operating with acceptable profits accompanied by an acceptable level of risk for shareholders' capital, likely gains considered.

Eventually, by maintaining unusual capital strength and liquidity, and by having a parent corporation which does likewise, Mutual Savings hopes to stand in particular favor with federal and state regulatory authorities and be in a position soundly to expand again, perhaps dramatically, and perhaps involving additional shareholder investment in Mutual Savings by the parent corporation.

Recent growth in savings accounts, considered on an incremental-effects basis, constitutes loss business, because Mutual Savings has incurred in interest and other expense more than it has received from employing proceeds in short-term interest-bearing investments far above regulatory requirements for liquidity. Moreover, some of the attendant expense may not have hit the books. In due course (starting in 1985) Mutual Savings, which with its large ratio of shareholders' equity to total liabilities imposes a virtually zero risk on FSLIC (the U.S. agency which insures safety of accounts in savings and loan associations), will be required to pay to FSLIC extra insurance premiums, based on Mutual Savings' gross size, to help fund FSLIC's protection of account holders in other savings and loan associations finally recognized as insolvent. In this process Mutual Savings, in effect, will retroactively pay extra interest-equivalent expense by reason of having attracted new savings. Mutual Savings' position at the moment is like that of a sober and careful automobile driver of 2000 miles per year, disadvantaged by his limited activity, yet forced to pay mutualized, standardized insurance premiums so long as he lives based on inclusion in a liability insurance pool (1) which is composed almost entirely of much worse risks, (2) which contains a considerable number of traveling salesmen previously convicted of drunk driving, and (3) which discovers liabilities, partly through institutional design, long after their occurrence. Deliberate growth in savings, under such conditions, reflects considerable optimism, perhaps Micawberish, that Mutual Savings will eventually have better ideas and opportunities and that its officers (including the Chairman) will make fewer of the sort of mistakes in which they participated in the past, leading to difficulties now decried.

The foregoing comments, designed to communicate reality for Wesco shareholders as it appears to Wesco management, should not be taken as criticism of FSLIC management. In recent years FSLIC management has bordered on heroic, considering economic and legal changes, political pressures, extraordinary work burden, novel problems and limited resources.

Precision Steel

Wesco's Precision Steel subsidiary, located in the outskirts of Chicago at Franklin Park, Illinois, was acquired for approximately $15 million on February 28, 1979. The price was roughly book value for a company which carried its inventories on a conservative LIFO accounting basis and which contained significant cash balances. More important, it had reached its position from a modest beginning through maintenance of sound, customer-oriented business values inculcated over a long time by a gifted founder and his successors. Precision Steel owns a well-established steel service center business and a subsidiary engaged in the manufacture and distribution of tool room supplies and other specialty metal products.

Precision Steel's businesses contributed $2,034,000 to "normal" net operating income in 1984, up 25% compared with $1,622,000 in 1983. Such a sharp increase in 1984 profit was not anticipated and was largely attributable to (1) increased sales (up 20% to $55,098,000) and (2) some favorable quantity-order prices on steel purchased.

Under the leadership of David Hillstrom, Precision Steel's businesses are now quite satisfactory, taking into account the financial leverage put into Wesco's consolidated picture incident to their acquisition. The 1984 year could be a hard act to follow.

Shortly after Wesco's purchase of Precision Steel, a substantial physical expansion of steel warehousing facilities was authorized, involving a new building in Charlotte, North Carolina. The new building and the whole North Carolina operation are now very successful, contributing $8,589,000 to sales in 1984 at a profit percentage higher than has prevailed in the long-established Chicago headquarters' facility.

Precision Steel's businesses, despite their mundane nomenclature, are steps advanced on the quality scale from mere commodity-type businesses. Many customers of Precision Steel, needing dependable supply on short notice of specialized grades of high-quality, cold-rolled strip steel, reasonable prices, technical excellence in cutting to order, and remembrance when supplies are short, rightly believe that they have no fully comparable alternative in Precision Steel's market area. Indeed, many customers at locations remote from Chicago and Charlotte (for instance, Los Angeles) seek out Precision Steel's service.

Wesco remains interested in logical expansion of Precision Steel's businesses, using liquid assets available.

All Other "Normal" Net Operating Income

All other "normal" net operating income, net of interest paid and general corporate expenses, rose to $4,550,000 in 1984 from $3,839,000 in 1983. Sources were (1) rents ($2,078,000 gross, excluding rent from Mutual Savings) from Wesco's Pasadena office building block (predominantly leased to outsiders although Mutual Savings is the ground floor tenant) and (2) interest and dividends from cash equivalents and marketable securities held by Precision Steel and its subsidiaries and at the parent company level.

Net Gains on Sales of Securities

Wesco's aggregate net gains on sales of securities, combined, after income taxes, increased to $13,138,000 in 1984 from $2,046,000 in 1983. The large 1984 gains do not indicate special acumen or good fortune in 1984. It merely happened that in 1984 unrealized appreciation occurring in previous years was cashed in.

A $1,080,000 portion of 1984 securities gains, if a different accounting treatment had been used, would have been both: (1) shifted to a different income category and (2) increased by $1,765,000. See next section.

Unusual Income and Certain Accounting Quirks in 1984 Reporting

Wesco's consolidated audited figures for net earnings contained in this Annual Report are lower by $1,328,000 in aggregate ($.19 per share) with respect to the nine months ended September 30, 1984, than the figures contained in Wesco's previously-issued quarterly reports covering such nine months.

The downward restatement of earlier reported earnings occurred because, after the close of the year, Wesco's outside auditor made an unanticipated interpretation of generally accepted accounting principles applicable to an unusual business transaction.

The unusual business transaction was cash paid by General Foods for transfer of General Foods' stock from Wesco to General Foods under a written arrangement with General Foods, specifying intention to create an exact dividend-equivalent, which kept Wesco's percentage ownership of General Foods the same at all times. Under such circumstances, income tax law quite naturally treats all proceeds of the in-form "sale" of General Foods stock as a dividend, which is the I.R.S. view as well as Wesco's view of the underlying economic substance. Last year, in a virtually identical case, Wesco's outside auditor approved, for the consolidated group of which Wesco is a part, financial statements including accounting treatment in conformity with in-substance dividend reporting to the I.R.S. and Wesco's 1984 quarterly reports of earnings followed this precedent with no objection. But, after much deliberation, the outside auditor's opinion early in 1985 came down in favor of treating the 1984 transactions with General Foods as sales instead of dividend-equivalents, except that income tax provision continued to be computed on the in-substance dividend basis.

From the Wesco shareholders' vantage point the result from the outside auditing decision made is that the error, if any, existing in the audited accounts by reason of the Wesco-auditor disagreement is now on the side of underreporting income. Wesco's audited net income for the full year 1984 is now lower by $1,765,000 ($.25 per share) than would have been reported if all proceeds of the 1984 business transaction with General Foods had been reported as unusual dividends or dividend-equivalents, following Wesco's view of substance. Either way, any income from the Wesco-General Foods business transaction is reported as "unusual" or from an irregular source (securities gains), and, either way, the 1984 year end balance sheet is exactly the same, except that in one case (Wesco's view) the after-tax balance sheet carrying cost would have been $1,765,000 higher for an identical number of General Foods' shares owned, with the $1,765,000 increase augmenting book net worth of Wesco.

While Wesco disagrees with its outside auditor on the accounting issue, Wesco can find something to applaud in (1) a de-emphasis of year-to-year consistency in search for an answer best in the auditor's latest view and (2) an auditor's favoring of a decision, where it has any doubt, which may err on the side of under-reporting income, considering a common tendency of corporate clients to favor decisions in the opposite direction.

Were Wesco running a national accounting partnership it would want a system where a high-ranked partner, free of business-retaining pressure, could reverse accounting decisions urged by field partners, so Wesco can hardly complain about the inconsistent messages from an audit-management system which forced Wesco in 1984 to change at year end quarterly income figures earlier reported. However, in this murky case, where we happen to know that one of the country's most eminent accountants agrees with the Wesco view, we must admit to minor irritation with the fates. Wesco makes special effort aimed at high-quality reporting to shareholders. (For instance, only with respect to competitively proprietary information, such as transactions in marketable securities, does Wesco consciously keep communication with shareholders to the legal minimum.) Thus when the audit quality-control system of its outside C.P.A. firm selects Wesco for forced restatement of numbers previously given shareholders, we feel much as if we were a duty-obsessed engineering student at Brigham Young University, accidentally tear-gassed by the national guard in a necessary program to control campus unrest.

The subject of this restatement of a small part of Wesco's earnings is covered at length here only because, much more often than not, it is a bad sign for shareholders when a full year-end audit decreases income reported as earned in previous quarterly reports. A full explanation is therefore appropriate.

The inconsistency between quarterly and final income figures is not the only accounting quirk in Wesco's audited 1984 financial statements. It seems odd, as highlighted above in the unconventional breakdown of earnings, that unrealized appreciation of $458,000 in a forward commitment to buy mortgage-equivalents was taken into Mutual Savings' income in 1984, which happened because the commitment was made in a futures market on a commodities exchange. A forward commitment to buy the same mortgage equivalents, made in some other manner, for instance by simple contract, would not, under the applicable accounting rules, result in the same unrealized appreciation's being reported as income. And, even though the unrealized appreciation is recognized as income in the 1984 earnings statement, shareholders must look deep into a footnote to the audited 1984 financial statements to find the only reference to the mortgage equivalents which produced the appreciation. The balance sheet standing alone discloses only short-term investments (U.S. Treasury Notes in this instance) the proceeds of which will be used in 1986 to close the forward commitment to buy the mortgage equivalents.

It also seems odd, in view of the substantial additional costs FSLIC membership will in the near future impose on Mutual Savings, that prepaid FSLIC premiums amounting to $3,146,000 are included in the audited consolidated balance sheet, without offset for anticipated new cost of sharing FSLIC liabilities. We do not object to the accounting convention at work. All complexities and interests considered, the accounting profession is doing all right by the civilization; the FSLIC relationship has long been a valuable asset in the savings and loan industry, with its mutualized nature of no practical adverse consequence; and both accounting and public-policy considerations disfavor quick invention of new accounting convention to anticipate in current financial statements future increases in burden from FSLIC membership by reason of facts already known.

But quirks (at least as diagnosed by Wesco) required (probably wisely, on balance) by accounting convention, do contribute to causing Wesco to break down and discuss its earnings unconventionally in its management letter and also to call shareholders' attention to audit footnotes. The use of both footnotes and letter is needed for a best-feasible understanding of economic reality as it appears to Wesco management.

It is recognized, of course, by most certified public accountants as well as by Wesco that audited statements alone, unless accompanied by a letter giving management's view of economic reality where inconsistent with the image created by accounting convention, is an improperly incomplete form of annual communication with corporate owners. There is a limit to the communication which properly standardized accounting can create, and Wesco's outside auditors (and its parent companies' auditors) over the years have been quite supportive of Wesco's approach to expanding numerate communication in the management letter, even though outside auditing jurisdiction.

Written arrangements creating the issue of unusual dividend-equivalent income, of the type which caused reporting quirks in 1984 as a result of transactions with General Foods, can hardly be expected to be made year after year. However, Wesco does anticipate, based on an agreement already signed, that in 1985 more of the same sort of transactions will occur with General Foods, probably somewhat smaller in aggregate amount than in 1984.

Consolidated Balance Sheet and Related Discussion

Wesco's consolidated balance sheet (1) retains a strength befitting a company whose consolidated net worth supports large outstanding promises to others and (2) reflects a continuing failure to acquire additional businesses because none are found available, despite constant search, at prices deemed rational when the interest of Wesco shareholders is taken into account.

As indicated in Note 2 to the accompanying financial statements, the aggregate market value of Wesco's marketable equity securities was higher than their aggregate cost at December 31, 1984 by about $13 million, down sharply from about $29 million one year earlier.

Wesco's Pasadena office building block (containing about 165,000 net rentable square feet including Mutual Savings' space) has a market value substantially in excess of carrying value, demonstrated by (1) mortgage debt ($5,182,000 at 9.25% fixed) against this real property now exceeding its depreciated carrying value ($3,069,000) in Wesco's balance sheet at December 31, 1984, and (2) substantial current net cash flow to Wesco after debt service on the mortgage.

Wesco remains in a prudent position when total debt is compared to total shareholders' equity and total liquid assets. Wesco's practice has been to do a certain amount of long-term borrowing in advance of specific need, in order to have maximum financial flexibility to face both hazards and opportunities.

It is expected that the balance sheet strength of the consolidated enterprise will in due course be used in one or more business extensions. The extension activity, however, requires some patience, as suitable opportunities are not always present.

As indicated in Schedule I accompanying Wesco's financial statements, common stock investments, both those in the savings and loan subsidiary and those held temporarily elsewhere pending sale to fund business extension, tend to be concentrated in a very few companies. Through this concentration practice better understanding is sought with respect to the few decisions made.

The ratio of Wesco's annual reported consolidated net income to reported consolidated shareholders' equity, about 13% in 1982-84, (1) was dependent to a considerable extent on securities gains, irregular by nature, and (2) nonetheless leaves something to be desired from the Wesco shareholders' point of view. Wesco began life as a savings and loan holding company in what became a very tough industry in which the real value, as distinguished from the reported book value, of most shareholders' equity became impaired, particularly in 1981-82. Damaged along with the rest of its industry, Wesco has been proceeding slowly under shortened sail, while it assesses damage and repairs the ship, instead of trying to make fast time by getting all canvas aloft. However, progress ultimately helpful to shareholders has not been restricted to what has shown up neatly in the income account covering this period. Increases over recent years in both (1) aggregate reported shareholders' equity and (2) the percentage of such equity outside Wesco's savings and loan segment are expected to be useful in the future.

On January 24, 1985, Wesco increased its regular quarterly dividend from 14½ cents per share to 15½ cents per share, payable March 7, 1985 to shareholders of record as of the close of business on February 19, 1985.

This annual report contains Form 10-K, a report filed with the Securities and Exchange Commission, and includes detailed information about Wesco and its subsidiaries as well as audited financial statements bearing extensive footnotes. As usual, your careful attention is sought with respect to these items.

Charles T. Munger

Charles T. Munger
Chairman of the Board

February 12, 1985

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 1984 — Commission file number 1-4720

WESCO FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	95-2109453
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
315 East Colorado Boulevard, Pasadena, California	91109
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (818) 449-2345

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Capital Stock, $1 par value	American Stock Exchange and Pacific Stock Exchange
10⅛% Notes Due 1991	American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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 twelve months and (2) has been subject to such filing requirements for the past 90 days. YES...X...No......

The aggregate market value of voting stock of the registrant held by non-affiliates of the registrant as of March 7, 1985 was: $29,123,628.

The number of shares outstanding of the registrant's Capital Stock as of March 7, 1985 was: 7,119,807.

DOCUMENTS INCORPORATED BY REFERENCE:

Title of Document	Parts of Form 10-K
Proxy Statement for 1985 Annual Meeting of Stockholders	Part III, Items 10, 11, 12 and 13

PART I

Item 1. Business

GENERAL

Wesco Financial Corporation ("Wesco") was incorporated in Delaware on March 18, 1959. The principal businesses of Wesco are the savings and loan business, through its wholly owned subsidiary, Mutual Savings and Loan Association ("Mutual Savings"), which was incorporated in California in 1925, and the steel service center business, through another wholly owned subsidiary, Precision Steel Warehouse, Inc. ("Precision Steel"). Wesco also has investments in real estate and marketable securities and owns a small insurance agency.

From 1973 to July 1983, Wesco was controlled by a corporation named Blue Chip Stamps. In July 1983, that company transferred ownership of its 80.1% investment in Wesco to a newly formed, wholly owned company (the present Blue Chip Stamps) and was subsequently merged into Berkshire Hathaway Inc. ("Berkshire"). Thus, Wesco and its subsidiaries are controlled and 80.1%-owned directly by the present Blue Chip Stamps and indirectly by Berkshire.

Wesco's activities fall into two business segments—financial and steel service. The financial segment includes the savings and loan business, operation of a business block in Pasadena, California, and investment in marketable common and preferred stocks. The steel service segment comprises mainly steel service center operations. The amounts of revenue, operating profit and identifiable assets attributable to each of these two business segments are contained in Item 6, Selected Financial Data, and Item 8, Financial Statements.

FINANCIAL SEGMENT

The earnings of Mutual Savings have historically been dependent on the interest rate spread between the yields earned on its long-term real estate loans and investments, and the costs of savings accounts and its other short-term borrowings.

The savings and loan business has been a difficult business in recent years, as institutions with substantial amounts of long-term, low-yielding mortgage loans on their books, funded by short-term borrowings from depositors, have seen their cost of funds increase dramatically. The increase in cost of funds has been due both to prevailing interest rates at levels much higher than were once thought normal, and to fundamental changes that have occurred in the savings and loan industry. As a result of changes in federal regulations affecting savings and loan associations (and other depository institutions such as banks), regulations limiting rate competition for depositors' accounts have been largely dismantled, and other regulations and regulatory attitudes have been modified to enable savings and loan associations and banks to compete more directly with each other and with other financial institutions in providing a wide variety of consumer financial services. This new environment thus far has not been very hospitable for the savings and loan business. In 1981 and 1982, most savings and loan associations suffered operating losses, and, although many have more recently earned profits, such profits have been earned principally as a result of the recent, and possibly short-term, moderation of interest rates. It is the belief of Wesco's management that such earnings may not be sustained so long as savings and loan associations continue their traditional practice of fixed-rate lending on a long-term basis (real estate loans) using short-term funds (savings accounts).

Mutual Savings has reacted to the changes in the savings and loan business by substantially reducing the size and scope of its business and altering the nature of its business activities. In 1979 Mutual Savings substantially curtailed its real estate loan originations because of the high cost of savings deposits, the reduction in net savings inflow, and uncertainty as to the future direction of loan interest rates. Though interest rates have moderated to some extent since early in 1983, Mutual Savings still does not engage in direct real estate lending to a significant extent since it still perceives risks and costs not adequately allowed for by present interest rate spreads.

In December 1980, Mutual Savings, which had operated at seventeen locations in Southern California and had ranked approximately 39th among California savings and loan associations in assets, sold all of its offices, except for its Pasadena headquarters office and a satellite office in a shopping mall across the street, to another association. Under terms of the sale, Mutual Savings transferred to the buyer approximately $307,000,000 of net branch savings accounts together with an equal book value of its highest-yielding mortgage loans and the physical assets of the branch offices, receiving approximately $8,000,000 in cash. Mutual Savings realized a gain on the sale of branch premises and equipment, after income taxes and expenses of sale, of $2,911,000.

In 1982, Mutual Savings sold approximately $13,000,000 of real estate loans backed by GNMA certificates, realizing a loss after income tax benefit of $2,425,000.

After the changes described above, the resulting savings and loan association is relatively small, ranking approximately 60th among California's savings and loan associations in assets at the end of 1984. Because it sold its highest-yielding mortgage loans in 1980, and it has not made many new loans at the higher interest rates that have prevailed since 1979, Mutual Savings is left with a fixed-rate mortgage portfolio bearing what may be the lowest average interest rate among all associations in the United States (7.6% per annum at the end of 1984). This remaining portfolio, carried on Mutual Savings' books at the end of 1984 at about $95,000,000, is worth substantially less at current interest rates. Compared to most other associations, Mutual Savings is believed to have a higher ratio of shareholders' equity to total interest-bearing liabilities; a higher proportion of assets in short-term, interest-bearing cash equivalents; and a much higher proportion of assets in intermediate-term, tax-exempt bonds and common and utility preferred stocks, producing a tax-equivalent yield substantially higher than that prevailing on the mortgage portfolio of the typical association.

Regulatory requirements and exhortations make it desirable for Mutual Savings to maintain at least 60% of its assets in mortgages, mortgage-equivalents, and other qualifying assets. Mutual Savings, in April 1984, agreed to buy in 1986 $30 million face amount of real estate loans, backed by GNMA certificates, at a price of approximately $19 million. These mortgages are expected to yield approximately 15% per annum on the agreed price.

Effective in January 1984 the regulations of the California Savings and Loan Commissioner were amended to provide that a savings and loan association could invest up to 5% of its assets in any securities deemed prudent by management of the association. As of December 31, 1984, Mutual Savings had invested the sum of $14,802,000 in common stocks under this authority.

Mutual Savings expects the savings and loan business to continue to be a difficult and competitive business. It intends to preserve its options by retaining financial strength and remaining very flexible with respect to expansion (including possible acquisition), contraction and revision of services designed to create more differentiation in the marketplace from standard financial services provided by others.

During 1984, Mutual Savings, excluding its service subsidiary, sustained a pre-tax operating loss before securities gains. However, the pre-tax loss was more than offset by income tax benefits available through application of Mutual Savings' pre-tax loss, as computed under income tax law, against pre-tax income of affiliates to be included in the same consolidated federal and state tax returns. In addition, the service subsidiary had a pre-tax operating profit before securities gains.

Effective in January 1983, the regulations of the California Savings and Loan Commissioner were amended to provide that a service corporation wholly owned by a savings and loan association could engage in any activity approved by the Commissioner. Mutual Savings' service subsidiary, Wes-Fin Service Corp. ("Wes-Fin"), accordingly obtained approval to purchase common and preferred stocks from time to time provided that, at the time of any purchase, the total amount invested would not exceed 7½% of the then total assets of Mutual Savings. As of December 31, 1984, Wes-Fin had invested the sum of $22,245,000 in common stocks under this authority.

Wesco, as a savings and loan holding company, and Mutual Savings, as a savings and loan association, are subject to regulation by federal and state authorities. Regulations relate to, among other things, reserve requirements, reporting requirements, periodic regulatory examinations, limitations on the types of loans and other investments that can be made, and the acquisition or disposition of certain types of businesses.

Wesco, while it seeks suitable additional businesses to acquire, invests in marketable common stocks of unaffiliated companies. (See Note 2 to the accompanying consolidated financial statements for a summary of these investments and Schedule I accompanying such statements for further information.) Wesco owns a business block in Pasadena, California, which includes the nine-story office building in which its headquarters and the main offices of Mutual Savings, Wes-Fin and WSC Insurance Agency (a small insurance agency wholly owned by Wesco) are located, and a multistory garage structure. These properties are nearly fully leased under agreements expiring at various dates to 1994.

Approximately 60 full-time employees are engaged in the savings and loan business and other financial segment activities.

STEEL SERVICE SEGMENT

Precision Steel, acquired by Wesco in 1979 for approximately $15,000,000, operates a well-established steel service center business in two service center locations: one in Franklin Park, Illinois, near Chicago; the other, operated by a wholly owned subsidiary, in Charlotte, North Carolina. The service centers buy low carbon sheet and strip steel, coated metals, spring steels, stainless steel, brass, phosphor bronze, aluminum and other metals, cut these metals to order, and sell them to a wide variety of customers.

The service center business is highly competitive. Precision Steel competes not only with other service centers but also with mills which supply metal to the service centers. Competition exists in the areas of price, quality, availability of products and speed of delivery. Because it is willing to sell in relatively small quantities, Precision Steel has been able to compete in geographic areas distant from its service center facilities.

Precision Brand Products, Inc. ("Precision Brand"), a wholly owned subsidiary of Precision Steel, manufactures shim stock and other tool room specialty items, as well as hose and muffler clamps, and distributes them under its own brand names nationwide, using both salesmen and manufacturers' representatives. This business is highly competitive.

Steel service raw materials are obtained principally from major domestic steel mills, and their availability is considered good. Precision Steel's service centers maintain extensive inventories in order to meet customer demand for prompt deliveries. Typically, an order is filled and the processed metals delivered to the customer within one week. Precision Brand normally maintains inventories adequate to allow for off-the-shelf service to customers.

The steel service businesses are subject to economic cycles; in 1983 they recovered from the adverse effect of the 1981-1982 recession. These businesses are not dependent on a few large customers. Steel service backlog orders increased to approximately $5,350,000 as of December 31, 1984 from approximately $4,400,000 as of December 31, 1983.

In 1980, Precision Brand introduced a line of precision measuring tools. As a result of poor acceptance by key distributors and end-users, coupled with recessionary economic conditions, the product line was discontinued in 1982 at a loss, after income taxes, of approximately $540,000.

Approximately 265 full-time employees are engaged in the steel service businesses, almost half of whom are members of unions. Management considers labor relations to be good.

Item 2. Properties

Wesco owns a business block in downtown Pasadena, California, which is improved with a nine-story office building that was constructed in 1964 and has approximately 124,000 square feet of net rentable area, as well as four commercial store buildings and a multistory garage with space for 425 automobiles. Approximately 22,000 square feet of this building are used by Wesco as its headquarters or leased to Mutual Savings for use as its main office, while the balance is leased to outside parties under agreements expiring at various dates to 1994. Mutual Savings leases its 1,700-square-foot satellite office in the Plaza Pasadena shopping center located across the street from its main office; this lease expires in 1990.

Mutual Savings holds real estate which has been acquired by foreclosure. The most valuable parcel consists of 22 acres of vacant, largely oceanfront land near Santa Barbara, California, where residential development is presently intended. Such development is subject to various difficult-to-obtain regulatory approvals, but the property is expected eventually to provide a yield greatly in excess of its book cost. Other properties include several buildings in a shopping center in Upland, California, which are leased to various small businesses, and repossessed land in Newhall, California; these properties are expected to be disposed of without significant gain or loss.

Precision Steel and its subsidiaries own three buildings, housing their plant and office facilities having usable area approximately as follows: 138,000 square feet in Franklin Park, Illinois; 42,000 square feet in Charlotte, North Carolina; and 59,000 square feet in Downers Grove, Illinois.

Item 3. Legal Proceedings

Wesco and its subsidiaries are not involved in any legal proceedings which could result in substantial loss.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of Wesco's shareholders subsequent to the annual meeting held in April 1984.

PART II

Item 5. Market for the Registrant's Common Stock and Related Stockholder Matters

Wesco's common stock is traded on the American Stock Exchange and the Pacific Stock Exchange.

The following table sets forth the ranges of stock prices reported in the Wall Street Journal for Wesco's shares trading on the American Stock Exchange by quarter for 1984 and 1983, as well as cash dividends paid by Wesco on each outstanding share:

	1984			1983		
	Sales Price		Dividends	Sales Price		Dividends
Quarter Ended	High	Low	Paid	High	Low	Paid
March 31	$19½	$16¼	$0.145	$15¾	$12	$0.135
June 30	19⅛	16½	0.145	19⅛	15½	0.135
September 30	19⅛	16⅜	0.145	20	16⅛	0.135
December 31	22⅝	17¾	0.145	17⅞	16⅞	0.135
			$0.58			$0.54

There were approximately 1,130 shareholders of record of Wesco's common stock as of the close of business on February 19, 1985.

Item 6. Selected Financial Data

Set forth below and on the following page are selected consolidated financial data for Wesco and its subsidiaries. For additional financial information, attention is directed to the footnote on the following page and to Wesco's audited 1984 consolidated financial statements appearing elsewhere in this report. (Dollar amounts are in thousands except for amounts per share.)

	Year Ended December 31,				
	1984	1983	1982	1981	1980
Financial:					
Revenues—					
Interest on loans*	$ 7,711	$ 8,567	$ 9,786	$ 12,211	$ 43,922
Interest on short-term investments and state and municipal bonds	17,170	9,294	8,975	8,597	8,150
Dividends on common and preferred stocks	7,765	9,025	8,298	7,904	6,244
Fluctuation in market value of GNMA futures contract	938	—	—	—	—
Gain (loss) on sale of marketable securities	19,360	3,025	9,998	2,643	(361)
Gain on sale of branches*	—	—	—	—	5,873
Other	1,952	1,787	2,204	1,566	2,661
	54,896	31,698	39,261	32,921	66,489
Expenses—					
Interest on savings accounts*	20,940	16,870	15,985	15,970	41,283
Interest on notes payable	3,103	4,673	6,199	6,778	7,180
General and administrative*	3,347	3,452	3,355	3,611	6,322
Loss on sale of loans	—	—	4,761	147	—
	27,390	24,995	30,300	26,506	54,785
Income before income taxes	27,506	6,703	8,961	6,415	11,704
Income tax (provision) benefit	(5,884)	2,228	2,214	1,417	(3,163)
Net income—financial	21,622	8,931	11,175	7,832	8,541
Steel service:					
Revenues—					
Sales	55,098	46,074	37,293	46,521	40,948
Other	207	191	189	465	126
	55,305	46,265	37,482	46,986	41,074
Costs and expenses—					
Cost of products sold	44,830	37,220	31,426	37,419	32,607
Selling, general and administrative expenses	6,501	5,936	5,492	6,018	5,513
	51,331	43,156	36,918	43,437	38,120
Income before income taxes	3,974	3,109	564	3,549	2,954
Income tax provision	(1,940)	(1,487)	(237)	(1,602)	(1,450)
Net income—steel service	2,034	1,622	327	1,947	1,504
Net income—consolidated	$ 23,656	$ 10,553	$ 11,502	$ 9,779	$ 10,045
Amounts per share:					
Net income—consolidated	$3.32	$1.48	$1.62	$1.37	$1.41
Cash dividends	$ .58	$ .54	$ .50	$ .46	$ .42

	December 31,				
	1984	1983	1982	1981	1980
Financial assets:					
Cash and short-term investments	$163,348	$ 69,262	$ 57,563	$ 31,201	$ 56,477
Common and preferred stocks and state and municipal bonds	126,179	142,427	119,845	123,755	105,875
Loans receivable*	95,172	106,886	123,541	149,656	164,648
Other assets	14,123	18,771	16,480	14,137	16,843
	398,822	337,346	317,429	318,749	343,843
Steel service assets	18,181	17,685	15,337	18,285	17,682
Total assets*	$417,003	$355,031	$332,766	$337,034	$361,525
Financial liabilities:					
Savings accounts*	$227,087	$188,195	$152,489	$149,168	$168,366
Notes payable	30,182	31,567	52,623	68,424	73,719
Other liabilities	10,850	5,907	6,394	5,810	12,048
	268,119	225,669	211,506	223,402	254,133
Steel service liabilities	5,245	5,250	3,857	4,171	4,435
Total liabilities*	$273,364	$230,919	$215,363	$227,573	$258,568
Shareholders' equity	$143,639	$124,112	$117,403	$109,461	$102,957
Per share	$20.17	$17.43	$16.49	$15.37	$14.46

*On December 1, 1980, Mutual Savings sold fifteen branch offices to Brentwood Savings and Loan Association, retaining two offices. Mutual Savings transferred approximately $307 million of net branch office savings deposits and an equal amount of its highest-yielding mortgage loans, together with the physical assets of the branch offices, receiving approximately $8 million in cash.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

FINANCIAL CONDITION

A glance at the consolidated balance sheet of Wesco Financial Corporation ("Wesco") and at the condensed consolidated balance sheet of its savings and loan subsidiary, Mutual Savings and Loan Association ("Mutual Savings"), appearing at the end of this annual report, will reveal the results of management's objective of increasing financial strength and liquidity. The increase in liquidity has been achieved as a result of a combination of factors. Mutual Savings has had success in increasing savings accounts since it began, in late 1982, offering savers (1) a slightly higher rate of interest than that paid by most other savings and loan associations on a new type of money-market account and (2) more competitive interest rates on other types of accounts. Mutual Savings' unusually high net worth (27 percent of savings accounts at 1984 yearend) has also enabled it to attract and retain savings deposits, as failures and near-failures of other savings and loan associations have drawn intensive press coverage.

Noteworthy developments that occurred in 1984 were (1) sales of marketable securities resulting in net gains of $13,138,000 after income taxes, and (2) the further decline ($11,711,000) of Mutual Savings' real estate loan portfolio due to its continued lending inactivity. In April 1984, however, Mutual Savings entered into a futures contract for the purchase in 1986 of $30 million of GNMA mortgage-backed pass-through certificates, at a cost of approximately $19 million. This forward commitment has been pre-funded by the purchase of U.S. Treasury Notes maturing at the approximate time that the purchase will close (see Item 1, Business).

The key component of a savings and loan association's earnings is net interest income. Its dependable generation not only requires the management of yields, costs and maturities of assets and liabilities, but also a limitation, consistent with the ratio of net worth to total interest-bearing liabilities, on the margin between interest-sensitive liabilities and interest-sensitive assets. This margin, or "gap," is typically negative in the savings and loan industry.

The table below sets forth the major balance sheet categories and dollar amounts of items in the Financial Segment as of 1984 yearend which are rate sensitive (i.e., cash flows are subject to reinvestment at then-prevailing interest rates).

Gap Analysis

	Amounts (in Thousands) Subject to Repricing(*)					
Balance Sheet Category	Within 6 months	Within 1 Year	Within 3 Years	Within 5 Years	Within 10 Years	Total
Cash and short-term investments	$119,148	$119,148	$119,148	$119,148	$119,148	$119,148
Intermediate-term U.S. Treasury Notes	—	—	44,200	44,200	44,200	44,200
State and municipal bonds	50	6,050	9,935	10,235	28,655	29,987
Common and preferred stocks	—	—	—	—	—	96,192
Loans receivable	4,000	8,000	23,000	35,000	60,000	95,172
Rate-sensitive assets	123,198	133,198	196,283	208,583	252,003	384,699
Savings accounts	148,124	177,916	226,754	227,036	227,087	227,087
Notes payable	28	60	198	363	25,942	30,182
Rate-sensitive liabilities	148,152	177,976	226,952	227,399	253,029	257,269
Net gap	$ (24,954)	$ (44,778)	$ (30,669)	$ (18,816)	$ (1,026)	$127,430

*Amounts are cumulative; for example, loans that can be repriced in one year include loans which can be repriced in six months.

The gap analysis demonstrates possibly temporary success in the ongoing restructuring of Wesco's financial operations, begun in the late 1970s, in order to reduce exposure to interest rate risk (see Item 1, Business). As now structured, Wesco's financial segment could very likely withstand sharp interest rate increases much better than most savings and loan holding companies and without extreme impact on operating income. Wesco can not predict its future responses, in terms of asset and maturity mixes, to opportunities and hazards presented in the future. Wesco will simply use its best judgment, all factors considered.

RESULTS OF OPERATIONS

Financial Segment

The last several years have seen dramatic, generally adverse changes in the savings and loan industry. In response, Wesco's savings and loan business has declined, both in size and in its relative importance to the financial segment. At the same time, as funds have become available pending their use in expansion or acquisition, the portfolio of marketable securities has grown, and dividend and interest income and gains and losses on securities transactions have increased in importance in Wesco's financial net income. Throughout this period of change, management's underlying objective has been sound business extension. (See Item 1, Business, for further discussion of the changes in the industry and of Wesco's financial segment.)

These strategic changes have resulted in less stability and predictability in Wesco's financial net income. The following summary demonstrates the prevalence of large, unusual items in recent years (amounts are in thousands of dollars, all after income tax effect):

	1984	1983	1982	1981	1980
Net financial income before unusual items	$ 8,026	$ 6,885	$ 6,894	$ 6,163	$ 5,800
Unusual items:					
Gain (loss) on sale of marketable securities	13,138	2,046	6,706	1,669	(170)
Fluctuation in market value of GNMA futures contract	458	—	—	—	—
Loss on sale of GNMA-backed real estate loans	—	—	(2,425)	—	—
Gain on sale of branches	—	—	—	—	2,911
	13,596	2,046	4,281	1,669	2,741
Financial net income, as reported in statements of income	$21,622	$ 8,931	$11,175	$ 7,832	$ 8,541

During 1984, Wesco and certain subsidiaries (the "Wesco Group") engaged in an unusual business transaction with General Foods Corporation ("General Foods") in connection with the latter's publicly announced share repurchase program in which $3,177,000 was paid by General Foods for transfer of General Foods' stock from the Wesco Group to General Foods under a written arrangement with General Foods specifying its intention to create an exact dividend-equivalent and keeping the Wesco Group's percentage ownership of General Foods the same at all times. Proceeds that were received through September 30, 1984 were reported by Wesco in quarterly reports for the second and third quarters as dividend income. Wesco's outside auditors, Peat, Marwick, Mitchell & Co., have subsequently interpreted generally accepted accounting principles applicable to this unusual business transaction to require its reporting as a sale of stock, notwithstanding (1) that the proceeds are taxed on an in-substance basis as dividend income and (2) that such in-substance tax treatment has been followed in computing Wesco's audited provision for taxes. As a result, a securities gain from the unusual transaction in the amount of $1,206,000, representing the proceeds after reduction for the assumed cost of the shares redeemed, but before income taxes, is included in gain on sale of marketable securities in the accompanying 1984 consolidated statement of income. (See Note 12 to the accompanying consolidated financial statements for further information, including the effects on quarterly earnings for the second and third quarters of 1984 resulting from the change in accounting treatment of the share redemption proceeds.)

Dividend income decreased during 1984 due to sales during the year of common stocks. Dividend income increased during 1983 due primarily to an increase in stocks held over the amount held in 1982.

Interest income on real estate loans declined dramatically in 1981 following Mutual Savings' disposition of $307,000,000 of real estate loans in connection with its sale of branch offices in December 1980. Moderate interest declines since 1981 have resulted mainly from the association's sale of $13,050,000 of GMNA-backed real estate loans in February 1982, and its continued inactivity in the real estate lending market.

Interest paid on savings deposits is dependent on the amount of savings on deposit and the interest rates paid on such deposits.

Interest rates that could be paid on short-term passbook-type accounts by federally regulated savings and loan associations such as Mutual Savings were, until about two years ago, kept at relatively low levels by federal regulation. Rates that could be paid on longer-term (certificate) accounts have, in recent years, generally been in excess of U.S. Treasury rates and have therefore been more competitive. Beginning in the late 1970s, when general market interest rates rose to unprecedented levels, depositors withdrew their short-term savings deposits en masse, shifting them to unregulated investments offering higher yields such as money market funds. This withdrawal of funds gave rise to the deregulation of interest rates paid by savings and loan associations on many types of accounts. In late 1982, following Mutual Savings' introduction of higher rates for savings, particularly on a new type of money market account, short-term funds began to return to Mutual Savings. Since 1982, savings accounts have grown by almost $75 million after having declined by almost $16 million in the two preceding years. (See Note 6 to the accompanying consolidated financial statements for a summary of the various savings accounts by interest rate as of 1984 and 1983 yearends.) On an incremental-effects basis recent growth in savings accounts has been at a loss, because Mutual Savings has incurred in interest and other expense more than it has received from employing proceeds in short-term interest-bearing investments far above regulatory requirements for liquidity.

Interest expense on savings accounts increased in 1984 over the amount paid during 1983, almost entirely the result of the increase in savings account balances during the year. In 1983, lower inflation was accompanied by lower interest rates. Thus, although the dollar amount of interest paid by Mutual Savings increased in 1983, the average rate of interest paid decreased from that of the prior year. This lowering of interest rates also reduced the previously high yield on short-term investments of Wesco's financial segment, adversely impacting the interest rate spread between combined yield on loans and investments and combined cost of savings and borrowings. With continuing deregulation of rates that may be paid to attract and retain most savings accounts, it is expected that competition for savings will increase, exerting a continuing pressure on the overall rate spread.

The following table sets forth the yield earned on loans and investments, the cost of savings and borrowings, and the interest rate spread between the combined weighted average yield on loans and investments and the combined weighted average cost of all funds for the past three years:

	1984	1983	1982
Yield on loans	7.63%	7.48%	7.42%
Yield on investments (a)	13.72	13.70	17.66
Combined yield on loans and investments	11.93	11.41	13.12
Cost of savings	(10.24)	(9.81)	(10.77)
Cost of borrowings	(9.83)	(9.73)	(9.66)
Combined cost of savings and borrowings	(10.18)	(9.79)	(10.44)
Rate spread (b)	1.75	1.62	2.68

(a) Interest on short-term investments, interest on state and municipal bonds and dividends on common and preferred stocks, all stated on a so-called tax-equivalent basis, i.e., on a pre-tax basis as if fully subject to income taxes at maximum corporate rates.

(b) The difference between the combined yield on loans and investments and the combined cost of savings and borrowings.

Although Wesco expects to continue to maintain a positive rate spread, the future of interest rates remains uncertain.

Interest expense on notes payable declined during 1984 and 1983 principally as a result of repayment of advances from the Federal Home Loan Bank.

Revenues of the financial segment include significant amounts of fully tax-exempt interest on state and municipal bonds, substantially exempt dividend income from common and preferred stocks, and gains and losses on sales of stock which are subject to favorable tax rates. The sale of $307,000,000 of loans to Brentwood Savings and Loan Association in December 1980 not only resulted in a significant drop in loan interest income, which is fully taxable, but provided capability to increase significantly investment income, which is partially or fully exempt. For this reason, and due to normal fluctuations in the investment income components, there have been tax provisions and benefits, expressed as percentages of pre-tax income, as follows: tax provisions of 21.4% in 1984 and 27.0% in 1980; tax benefits of 33.2% in 1983, 24.7% in 1982 and 22.1% in 1981. (See Note 8 to the accompanying consolidated financial statements for further information on income taxes.)

Revenues, expenses and earnings set forth in Item 6, Selected Financial Data, and in Wesco's consolidated statement of income are not necessarily indicative of future revenues, expenses and earnings in that they are subject to variations and timing of securities gains and losses, the occurrence of other unusual items and changes in the interest rate spread.

Steel Service Segment

Sales revenues of the steel service group increased in each of the two most recent years mainly as a result of the general economic resurgence experienced since the 1981-1982 economic recession.

Cost of products sold, as a percentage of sales, was somewhat higher in 1982 than in 1983 or 1984 due principally to the inclusion in the 1982 figure of a pre-tax loss of $1,075,000 from discontinuation of a precision measuring tool product line. The product line had been introduced in 1980 but had met with poor acceptance by key distributors and end-users coupled with recessionary economic conditions.

Selling, general and administrative expenses include compensation and other expenses which vary in accordance with sales volume.

The provision for income taxes in the steel service segment, although it fluctuated in amount, represented 48.8%, 47.8%, and 42.0% of pre-tax income for 1984, 1983 and 1982, respectively, not significantly different from the combined federal and state rates on ordinary income.

Item 8. Financial Statements

Following is an index to financial statements appearing in this report:

The data appearing on the financial statement schedules listed below should be read in conjunction with the consolidated financial statements and notes of Wesco Financial Corporation and the reports of independent accountants referred to above. Schedules not included with these financial statement schedules have been omitted because they are not applicable or the required information is shown in the financial statements or notes thereto.

Item 9. Disagreements on Accounting and Financial Disclosure

Effective July 28, 1983, Blue Chip Stamps, parent of Wesco, was merged into Berkshire Hathaway Inc. ("Berkshire"). Prior to that time, Blue Chip Stamps and Wesco retained the services of Price Waterhouse as their independent public accounting firm. Berkshire retained the services of Peat, Marwick, Mitchell & Co. Thereafter, Wesco's Audit Committee found it desirable that the same accounting firm that handles Berkshire should also handle all the subsidiaries of Berkshire, including Wesco. They therefore recommended the appointment of Peat, Marwick, Mitchell & Co. as auditor for Wesco and its subsidiaries. There were no disagreements with Price Waterhouse on any matters of accounting principles or practices or financial statement disclosure.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information set forth in the section entitled "Election of Directors" appearing on pages 2, 3 and 4 of the definitive combined notice of annual meeting and proxy statement of Wesco Financial Corporation dated March 28, 1985, is incorporated herein by reference.

Item 11. Management Remuneration and Transactions

The information set forth in the section "Compensation of Directors and Executive Officers" appearing on pages 6 and 7 of the definitive combined notice of annual meeting and proxy statement of Wesco Financial Corporation dated March 28, 1985, is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information set forth in the section "Voting Securities and Principal Holders Thereof" appearing on pages 4 and 5 of the definitive combined notice of annual meeting and proxy statement of Wesco Financial Corporation dated March 28, 1985, is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

The information set forth in the section "Transactions With Management and Others" appearing on page 8 of the definitive combined notice of annual meeting and proxy statement of Wesco Financial Corporation dated March 28, 1985, is incorporated herein by reference.

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

The index to financial statements set forth in Item 8 of this report is incorporated herein by reference.

The following exhibits (listed by numbers corresponding to Table 1 of Item 601 of Regulation S-K) are incorporated herein by reference:

3a. Articles of Incorporation and By-Laws of Wesco Financial Corporation (incorporated by reference to Form 10-K Annual Report of Wesco Financial Corporation for the year ended December 31, 1980).

4. Form of Indenture (incorporated by reference to Exhibit 2 to Amendment No. 1 of Form S-7 Registration Statement of Wesco Financial Corporation filed June 20, 1979. File No. 2-64616).

22. Subsidiaries.

No reports on Form 8-K were filed during the quarter ended December 31, 1984.

SIGNATURES

Pursuant to the requirements of Section 13 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.

WESCO FINANCIAL CORPORATION

By:

Charles T. Munger — March 28, 1985
Chairman of the Board and President
(principal executive officer)

By:

Jeffrey L. Jacobson — March 28, 1985
Vice President and Chief Financial Officer
(principal financial officer)

By:

Jeanne Leach — March 28, 1985
Treasurer
(principal accounting officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Charles T. Munger — March 28, 1985
Director

H. R. Dettmann — March 28, 1985
Director

David K. Robinson — March 28, 1985
Director

James N. Gamble — March 28, 1985
Director

REPORTS OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Shareholders of
Wesco Financial Corporation

We have examined the consolidated financial statements of Wesco Financial Corporation and subsidiaries as of and for the years ended December 31, 1984 and 1983, as listed in the accompanying index under Item 8. Our examinations were 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. In connection with our examination of the consolidated financial statements, we also examined the supporting schedules as of and for the years ended December 31, 1984 and 1983, as listed in the accompanying index under Item 8.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Wesco Financial Corporation and subsidiaries at December 31, 1984 and 1983, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis. Also, in our opinion, the related supporting schedules as of and for the years ended December 31, 1984 and 1983, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

Peat, Marwick, Mitchell & Co.

Los Angeles, California
January 31, 1985

To the Board of Directors and Shareholders of
Wesco Financial Corporation

In our opinion, the consolidated financial statements listed in the accompanying index under Item 8 present fairly the results of operations and the changes in financial position of Wesco Financial Corporation and its subsidiaries for the year ended December 31, 1982, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. This opinion is based on an examination which was made by us 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.

Price Waterhouse

Los Angeles, California
February 17, 1983

WESCO FINANCIAL CORPORATION
CONSOLIDATED BALANCE SHEET
(Dollar amounts in thousands)

ASSETS	December 31, 1984	December 31, 1983
Financial:		
Cash	$ 1,951	$ 2,125
Short-term investments (Note 2)	161,397	67,137
State and municipal bonds (Note 2)	29,987	30,958
Common and preferred stocks (Note 2)	96,192	111,469
Loans receivable (Note 3)	95,172	106,886
Interest and dividends receivable	2,681	2,623
Income taxes receivable (Note 8)	—	2,596
Real estate held for sale	2,011	4,480
Investments required by law:		
Investment in stock of Federal Home Loan Bank, at cost	1,137	1,149
Prepayments to FSLIC secondary reserve	3,146	2,879
Premises and equipment, net (Note 4)	3,216	3,308
Other assets	1,932	1,736
	398,822	337,346
Steel service:		
Cash	13	13
Accounts receivable	5,318	5,358
Inventories (Note 5)	7,690	6,893
Property, plant and equipment, net (Note 4)	5,080	5,299
Other assets	80	122
	18,181	17,685
	$417,003	$355,031

LIABILITIES AND SHAREHOLDERS' EQUITY	1984	1983
Financial:		
Savings accounts (Note 6)	$227,087	$188,195
Notes payable (Note 7)	30,182	31,567
Accounts payable and accrued expenses	5,047	1,253
Income taxes payable, principally deferred (Note 8)	5,803	4,654
	268,119	225,669
Steel service:		
Notes payable (Note 7)	1,700	1,920
Accounts payable and accrued expenses	2,259	2,238
Income taxes payable (Note 8)	1,286	1,092
	5,245	5,250
Total liabilities	273,364	230,919
Commitments and contingent liabilities (Notes 9 and 10)		
Shareholders' equity:		
Capital stock, $1 par value—authorized 7,500,000 shares; issued 7,119,807 shares	7,120	7,120
Capital surplus arising from stock dividends	23,319	23,319
Retained earnings—partially restricted (Note 11)	113,200	93,673
Total shareholders' equity	143,639	124,112
	$417,003	$355,031

See accompanying notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION
CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS
(Dollar amounts in thousands except for amounts per share)

	Year Ended December 31, 1984	1983	1982
Financial:			
Revenues—			
Interest on loans	$ 7,711	$ 8,567	$ 9,786
Interest on short-term investments and on state and municipal bonds	17,170	9,294	8,975
Dividends on common and preferred stocks	7,765	9,025	8,298
Fluctuation in market value of GNMA futures contract (Note 3)	938	—	—
Gain on sales of marketable securities	19,360	3,025	9,998
Rental income of $2,078, $1,986 and $1,867, less expense of $1,032, $1,051 and $1,007	1,046	935	860
Other	906	852	1,344
	54,896	31,698	39,261
Expenses—			
Interest on savings accounts	20,940	16,870	15,985
Interest on notes payable	3,103	4,673	6,199
General and administrative	3,347	3,452	3,355
Loss on sale of loans	—	—	4,761
	27,390	24,995	30,300
Income before income taxes	27,506	6,703	8,961
Income tax (provision) benefit (Note 8)	(5,884)	2,228	2,214
Net income—financial	21,622	8,931	11,175
Steel service:			
Revenues—			
Sales	55,098	46,074	37,293
Other	207	191	189
	55,305	46,265	37,482
Costs and expenses—			
Cost of products sold	44,830	37,220	31,426
Selling, general and administrative expenses	6,501	5,936	5,492
	51,331	43,156	36,918
Income before income taxes	3,974	3,109	564
Income tax provision (Note 8)	(1,940)	(1,487)	(237)
Net income—steel service	2,034	1,622	327
Net income—consolidated	23,656	10,553	11,502
Retained earnings—beginning of year	93,673	86,964	79,022
Cash dividends declared and paid	(4,129)	(3,844)	(3,560)
Retained earnings—end of year	$113,200	$ 93,673	$ 86,964
Amounts per share based on 7,119,807 shares:			
Net income—consolidated	$3.32	$1.48	$1.62
Cash dividends	$ .58	$ .54	$ .50

See accompanying notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
(Dollar amounts in thousands)

	Year Ended December 31,		
	1984	1983	1982
Financial:			
Sources (uses) of cash, including short-term investments, from operations—			
Net income	$21,622	$ 8,931	$11,175
Add (deduct):			
Depreciation and amortization, including amortization of bond premiums of $421, $421 and $416	721	765	843
Interest expense credited to savings accounts	18,061	15,537	11,071
(Increase) decrease in current income taxes receivable	2,596	(91)	(2,505)
Increase (decrease) in income taxes payable	1,012	(268)	817
Net loss on sale of GNMA-backed loans	—	—	2,425
Other, net	(880)	(517)	(1,476)
Cash provided from financial operations	43,132	24,357	22,350
Other sources (uses) of cash—			
Principal collections on real estate loans, net	11,396	15,097	11,943
Proceeds from sale of GNMA-backed loans, net of related tax benefit	—	—	10,623
Increase (decrease) in savings accounts and repurchase agreements, net	20,831	20,169	(7,750)
(Increase) decrease in state and municipal bonds and common and preferred stocks	16,248	(23,024)	3,465
Decrease in loans on savings accounts, net	318	1,558	1,197
Increase in accounts payable from purchases of common stocks	4,012	—	—
(Increase) decrease in real estate held for sale	2,469	(2,754)	—
Proceeds from sale of FHLB stock	152	860	1,083
Repayment of notes payable	(1,385)	(21,056)	(15,801)
Payment of cash dividends	(4,129)	(3,844)	(3,560)
Other, net	(468)	(331)	(149)
	92,576	11,032	23,401
Steel service:			
Sources (uses) of cash from operations—			
Net income	2,034	1,622	327
Add (deduct):			
Depreciation and amortization	650	633	614
Decrease (increase) in receivables	40	(1,661)	1,109
Decrease (increase) in inventories	(797)	(1,524)	1,613
Increase (decrease) in accounts payable and accrued expenses	21	842	(182)
Increase (decrease) in income taxes payable	194	769	(83)
Other, net	41	28	37
Cash provided from steel service operations	2,183	709	3,435
Other uses of cash—			
Additions to property, plant and equipment	(453)	(148)	(315)
Repayment of notes payable	(220)	(218)	(49)
	1,510	343	3,071
Consolidated increase in cash, including short-term investments	$94,086	$11,375	$26,472

See accompanying notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands except for amounts per share)

Note 1. Presentation and Consolidation

The consolidated financial statements of Wesco Financial Corporation ("Wesco") are classified according to the consolidated group's two business segments—financial and steel service.

The financial segment of the consolidated financial statements includes the accounts of Wesco and its wholly owned subsidiaries, Mutual Savings and Loan Association ("Mutual Savings") and WSC Insurance Agency, together with Mutual Savings' wholly owned subsidiary, Wes-Fin Service Corp.

The steel service segment of the consolidated financial statements includes the operating accounts of Precision Steel Warehouse, Inc. ("Precision Steel") and its wholly owned subsidiaries, Precision Brand Products, Inc., and Precision Steel Warehouse, Inc.—Charlotte Service Center. Short-term investments and investments in common stocks, together with related interest and dividend income and gain or loss on related sales, are included in the financial segment.

Wesco is 80.1%-owned by Blue Chip Stamps, which in turn is wholly owned by Berkshire Hathaway Inc. ("Berkshire").

All material intercompany balances and transactions have been eliminated.

Note 2. Investments in Marketable Securities

Following is a summary of marketable securities at yearend:	1984		1983	
	Cost	Market	Cost	Market
Short-term investments	$161,397	$164,527	$ 67,137	$ 67,137
State and municipal bonds	$ 29,987	$ 32,543	$ 30,958	$ 33,230
Marketable equity securities—				
Common stocks	$ 65,862	$ 80,177	$ 81,139	$111,890
Preferred stocks	27,724	26,349	27,724	26,236
	93,586	106,526	108,863	138,126
Other preferred stocks	2,606	2,334	2,606	2,416
	$ 96,192	$108,860	$111,469	$140,542

At December 31, 1984, the consolidated portfolio of marketable equity securities contained aggregate unrealized gains of $14,958 and aggregate unrealized losses of $2,018.

Common and preferred stocks are stated at the lower of aggregate cost (first-in, first-out) or market on the consolidated balance sheet. Short-term investments (mainly securities issued by the U.S. Government and its agencies) are stated at cost, adjusted for amortization of premium and accretion of discount.

Note 3. Loans Receivable

Following is a summary of loans receivable by type of collateral at yearend:	1984	1983
Residential property of one to four units	$ 80,329	$ 89,532
Residential property of more than four units	11,147	12,491
Commercial property and vacant land	3,275	4,201
Savings accounts	493	811
	95,244	107,035
Less unearned loan fees, unrealized profit on sales of real estate and undistributed loan funds	(72)	(149)
	$ 95,172	$106,886
Average interest rate	7.63%	7.48%

Interest income on loans is recognized under the accrual method of accounting. Such accrued interest amounted to $368 and $458 at 1984 and 1983 yearends.

Mutual Savings entered into a financial futures contract in April 1984 for the purchase in March 1986 of $30 million principal amount of GNMA mortgage-backed pass-through certificates, at a cost of approximately $19 million to be paid in 1986. Management believes that the certificates will yield approximately 15% based on cost. Generally accepted accounting principles require that earnings reflect fluctuations in market value of futures contracts. The unrealized gain as of December 31, 1984, of $938 before income taxes, is reflected on the accompanying consolidated statement of income in the category fluctuation in market value of GNMA futures contract.

Note 4. Property, Plant, Premises and Equipment

Following is a summary of property, plant, premises and equipment, stated at cost, at yearend:

	1984	1983
Financial:		
Land	$1,386	$1,386
Office, store and garage buildings and leasehold improvements	6,217	6,035
Furniture, fixtures and equipment	832	866
	8,435	8,287
Less accumulated depreciation and amortization	5,219	4,979
	$3,216	$3,308
Steel service:		
Land	$ 640	$ 640
Buildings and improvements	2,907	2,873
Machinery and equipment	4,729	4,385
	8,276	7,898
Less accumulated depreciation and amortization	3,196	2,599
	$5,080	$5,299

The financial and a portion of the steel service land and buildings secure certain debt. See Note 7.

Property, plant, premises and equipment are depreciated under the straight-line method over the estimated useful lives of the assets.

Note 5. Inventories

Inventories of the steel service group are valued at the lower of last-in, first-out ("LIFO") cost or market. If the first-in, first-out ("FIFO") method of determining inventory cost had been used in lieu of the LIFO method, inventories would have been higher by $4,900 and $4,568 at yearend in 1984 and 1983.

An increase in steel service center inventory quantities in 1984 resulted in an increase in LIFO inventory quantities carried at costs prevailing in prior years which were lower than costs at yearend in 1984, the effect of which decreased 1984 net income by approximately $167 or $.02 per Wesco share.

30 Dollar amounts in thousands except for amounts per share

Note 6. Savings Accounts

Following is a summary of savings accounts by type of account and interest rate at yearend:

Type of Account	Interest Rate	1984	1983
Interest-bearing checking accounts[a]	5.25%	$ 1,586	$ 1,453
Passbook accounts[a]	5.50	14,771	19,551
Money market rate accounts[a]	9.23[d]	56,207	61,502
Certificate accounts:			
7–31 days	9.09	517	1,095
32 days–6 months	11.14	25,180	6,086
6 months[b]	11.73[c,d]	8,181	20,655
7 months–1 year	11.18	8,760	3,152
13 months–2 years	11.23	23,621	5,172
18 months[b]	11.06[c,d]	5,146	3,247
25 months–4 years	11.44	42,235	15,855
30 months[b]	11.92[c,d]	11,784	30,265
4 years[b]	7.50	1,074	1,797
6 years[b]	7.75	933	3,578
8 years[b]	8.00	1,337	1,510
IRA/Keogh accounts, 18 months[e]	11.81[d]	12,677	7,122
Jumbo certificates of deposit	11.67[d]	10,952	4,720
Other accounts	9.93	2,125	1,435
		$227,086	$188,195

[a] No stated maturity.
[b] No longer offered.
[c] Interest tied to U.S. Treasury bill rates.
[d] Weighted average interest rate at yearend 1984.
[e] Other IRA/Keogh accounts included in the various certificate accounts amounted to $2,967 and $2,844 at 1984 and 1983 yearends.

The weighted average interest rates on all accounts at 1984 and 1983 yearends were 10.37% and 9.82%. These rates are based upon stated interest rates without giving consideration to daily compounding of interest or forfeiture of interest due to premature withdrawals.

At yearend in 1984 certificate accounts mature as follows: 1985, $105,352; 1986, $38,806; 1987, $5,258; 1988, $4,774; 1989, $196; thereafter, $136.

Note 7. Notes Payable

Following is a list of notes payable at yearend:

	1984	1983
Wesco—		
Notes due June 1991, currently redeemable at 105% of face value declining to 100% by 1989, bearing interest at 10⅛%, payable in semiannual installments	$25,000	$25,000
Notes payable, secured by land, buildings and assignment of leases, due in monthly installments through February 2007 of $45 including interest at 9¼%	5,182	5,166
Mutual Savings—Federal Home Loan Bank advances	—	1,401
Total financial	$30,182	$31,567
Precision Steel—		
Industrial revenue bonds, guaranteed by Wesco, due in quarterly installments through December 1994 of $42 plus interest at 6½%	$ 1,665	$ 1,833
Notes payable, secured by land and buildings, due in monthly installments through July 1985 of $5 including interest at 5½%	35	87
Total steel service	$ 1,700	$ 1,920

Dollar amounts in thousands except for amounts per share 31

Notes payable at yearend in 1984 mature as follows:

Year	Consolidated Financial	Steel Service
1985	$ 60	$ 199
1986	66	167
1987	72	167
1988	78	167
1989	87	167
Thereafter	29,819	833
	$30,182	$ 1,700

Agreements relating to the 10⅛% notes and the industrial revenue bonds contain covenants, among others, restricting funded debt, dividends and liens on property, plant and equipment. The obligors are in compliance with all of the covenants.

Note 8. Taxes on Income

The consolidated statement of income contains income tax charges (benefits) as follows:

	1984	1983	1982
Applicable to:			
Financial	$ 5,884	$(2,228)	$(2,214)
Steel service	1,940	1,487	237
	$ 7,824	$ (741)	$(1,977)

These taxes are payable or recoverable as follows:

	1984	1983	1982
Payable (recoverable) currently—			
Federal	$ 5,179	$ (977)	$(3,694)
State	2,634	504	192
	7,813	(473)	(3,502)
Payable (recoverable) in the future—			
Federal	(9)	(279)	1,117
State	20	11	408
	11	(268)	1,525
	$ 7,824	$ (741)	$(1,977)

Of the above taxes, the amounts currently recoverable are included in income taxes receivable and the amounts currently payable are included in income taxes payable on the consolidated balance sheet, after deducting estimated payments. The amounts payable or recoverable in the future are included in deferred income taxes on the consolidated balance sheet, and result from the following timing differences in the recognition of revenue and expense items in the tax returns as compared to the financial statements:

	1984	1983	1982
Loan fees recognized under a different method for tax purposes	$ (316)	$ (435)	$ 1,342
State income taxes deducted on cash basis for tax purposes vs. accrual basis on the books	(959)	(724)	(424)
Mutual Savings' income recognized on cash basis for tax purposes vs. accrual basis on the books	230	(18)	194
Other timing differences	1,056	909	413
Total taxes payable (recoverable) in the future	$ 11	$ (268)	$ 1,525

Dollar amounts in thousands except for amounts per share

The income tax provision of $7,824 for 1984 amounted to 24.9% of pre-tax income of $31,480, the benefit of $741 for 1983 represented 7.6% of pre-tax income of $9,812, and the benefit of $1,977 for 1982 represented 20.8% of pre-tax income of $9,525. Following is a summary of the differences between the federal statutory rate and these effective income tax rates:

	1984	1983	1982
Statutory federal income tax rate	46.0%	46.0%	46.0%
Increase (decrease) resulting from:			
85% exclusion from taxable income of dividends on common and preferred stocks and on securities gains taxable as dividend-equivalents	(11.1)	(36.0)	(34.1)
100% exclusion from taxable income of interest on state and municipal bonds	(4.7)	(15.1)	(17.4)
Use of lower rate on capital gains	(9.9)	(5.5)	(18.9)
State income taxes, net of federal income tax benefit	4.6	2.4	3.4
Other differences, net	—	.6	.2
Effective income tax (benefit) rate	24.9%	(7.6)%	(20.8)%

Investment tax credits are recognized as the tax benefits are realized.

Prior to 1983, Wesco and its subsidiaries were included in consolidated federal returns filed by a corporation named Blue Chip Stamps. In July 1983, that company transferred ownership of its 80.1% investment in Wesco to a newly formed, wholly owned company (the present Blue Chip Stamps) and was subsequently merged into Berkshire Hathaway Inc. (Berkshire). Thus, Wesco and its subsidiaries are indirectly 80.1% owned by Berkshire and are included in the latter's consolidated federal income tax returns.

The provision (or benefit) for federal income tax is computed on the separate results of operations of Wesco as if it filed a separate consolidated return, and the amounts and timing of cash settlements between Wesco and Berkshire are made under the same assumption.

Federal income tax returns through 1979 have been examined by and settled with the Internal Revenue Service.

Dollar amounts in thousands except for amounts per share 33

Note 9. Lease Commitments and Rental Expense

At yearend in 1984, Wesco and its subsidiaries have future minimum rental commitments as follows: 1985, $369; 1986, $340; 1987, $316; 1988, $316; 1989, $225; thereafter, $9. Rental expense amounted to $456, $421, and $463 in 1984, 1983, and 1932.

Note 10. Pension and Profit Sharing Plans

A noncontributory retirement plan is in effect for all eligible employees of the companies included in the financial segment. Annual employer contributions to the fund are computed actuarially utilizing the aggregate-cost funding method. Pension costs for 1984, 1983 and 1982 amounted to $60, $52 and $57.

Precision Steel and the other companies comprising the steel service segment contribute to retirement plans covering substantially all employees. Precision Steel administers three plans. One plan covers certain hourly employees. Two plans cover eligible nonunion salaried employees: one is a pension plan for which retirement benefits were frozen and became fully vested in 1982; the other is a profit sharing plan enacted at that time. Contributions are also made to two multi-employer union-administered pension plans.

Contributions for Precision Steel-administered pension plans are funded annually at amounts calculated actuarially to cover normal costs for both plans and amortization of prior service costs over 34 years for the salaried plan. Contributions to the profit sharing plan are based upon a defined contribution formula. Contributions to the union-administered plans are based on negotiated hourly rates. Pension costs for 1984, 1983 and 1982 were $162, $158, and $4.

Set forth below is a comparison of accumulated benefits with net assets available for payment of such benefits for the employer-sponsored defined benefit pension plans as of July 1, 1983 for the financial segment and June 1, 1984 for the steel service segment (the most recent actuarial valuations). The rates of return assumed in determining present values ranged from 6% to 7%.

	Financial	Steel Service
Actuarial present value of accumulated plan benefits:		
Vested	$ 675	$1,544
Nonvested	10	121
	$ 685	$1,665
Net assets available for benefits	$1,167	$1,853

Dollar amounts in thousands except for amounts per share

Note 11. Retained Earnings

The Federal Savings and Loan Insurance Corporation ("FSLIC") requires savings and loan associations to maintain certain reserves which may be used only for the purpose of absorbing loan losses. In addition, associations must maintain certain reserves under California law. Such reserve requirements, which amounted to $35,178 at December 31, 1984, represent a restriction of retained earnings. These reserves are not related to amounts of losses actually anticipated and have not been charged against book income.

The $35,178 of statutory bad debt reserves, together with $12,136 of retained earnings appropriations not similarly restricted as to dividends, were taken as special bad debt deductions for tax purposes through 1968, after which such deductions were no longer available to Mutual Savings due to its having reached certain limitations. Provision for income taxes has not been made with respect to these amounts; if, in the future, any portion is used for any purpose other than to absorb loan losses, including payment of dividends or distribution in liquidation, such withdrawal will necessitate accrual and payment of income taxes.

Because of the special bad debt deductions, and other differences in methods of reporting results of operations for tax return and financial statement purposes, Mutual Savings' ability to pay dividends to Wesco without being subject to tax is limited to approximately $10,000, plus future earnings on a tax-return basis (no dividends were paid in 1984 or 1983, and only $1,000 in 1982).

A summary of consolidated retained earnings follows:

Statutory reserve	$ 35,178
Retained earnings available for cash dividends:	
Subject to federal income taxes	12,136
Not subject to federal income taxes	65,886
	78,022
Retained earnings at December 31, 1984	$113,200

Dollar amounts in thousands except for amounts per share 35

Note 12. Quarterly Financial Information

Unaudited quarterly financial information for 1984 and 1983 follows. Information for the second and third quarters of 1984 is restated from that previously presented, reflecting a changed accounting treatment of General Foods share redemption proceeds received during those periods (see below).

	Quarter Ended			
	December 31, 1984	September 30, 1984	June 30, 1984	March 31, 1984
Financial revenues	$10,160	$19,228	$17,151	$ 7,305
Interest expense—savings accounts	(5,810)	(5,177)	(5,073)	(4,880)
Steel service revenues	12,941	13,190	14,183	14,991
Cost of steel products sold	(10,217)	(10,806)	(11,597)	(12,210)
Net income	3,400	9,213	8,797	2,246
Per share	.47	1.29	1.24	.32
Securities gains, less securities losses, net of income tax effect, included in net income above	348	5,848	6,942	—
Per share	.05	.82	.97	—
	December 31, 1983	September 30, 1983	June 30, 1983	March 31, 1983
Financial revenues	$ 7,517	$ 7,279	$ 7,238	$ 9,664
Interest expense—savings accounts	(4,480)	(4,306)	(4,022)	(4,062)
Steel service revenues	12,156	11,742	11,530	10,837
Cost of steel products sold	(9,361)	(9,552)	(9,385)	(8,922)
Net income	2,307	2,190	2,321	3,735
Per share	.32	.31	.33	.52
Securities gains, less securities losses, net of income tax effect, included in net income above	—	—	157	1,889
Per share	—	—	.02	.26

In the second and third quarters of 1984, Wesco and certain subsidiaries (the "Wesco Group") received approximately $1.3 million and $1.1 million, respectively, representing proceeds from redemption by General Foods Corporation of its shares owned by the Wesco Group. The redemptions by General Foods of its shares owned by the Wesco Group were made pursuant to contractual arrangements whereby the redemptions kept unchanged the Wesco Group's ownership percentages of total General Foods outstanding shares. The proceeds distributed by General Foods to the Wesco Group in the form of redemption of General Foods shares were, economically to the Wesco Group, substantially equivalent to dividend income.

In its second and third quarter 1984 financial reports, Wesco applied the substance-over-form principle in accounting for the proceeds received as dividend income. Income previously reported for 1984 interim periods was not reduced for the original cost of the redeemed shares. Wesco's independent accountants subsequently advised the Company that its substance-over-form view does not provide, in the accountants' judgment, a proper basis under generally accepted accounting principles to account for the proceeds as dividend income. Earnings data for the second and third quarters of 1984 are accordingly restated in the above summary to reflect the General Foods share redemption proceeds, after reduction for cost of shares redeemed, as realized investment gain. The after-tax effect of the change is to reduce earnings from amounts previously reported for the second quarter by $763 ($.11 per share), and for the third quarter by $565 ($.08 per share).

Dollar amounts in thousands except for amounts per share

WESCO FINANCIAL CORPORATION
SCHEDULE I—MARKETABLE SECURITIES

DECEMBER 31, 1984
(Dollar amounts in thousands)

Name of Issuer and Title of Each Issue	Number of Shares of Stock or Principal Amount of Notes	Cost of Each Issue (Amount on Balance Sheet)	Market Value of Each Issue at Balance Sheet Date
Securities held by the consolidated group were as follows:			
Securities of U.S. Government and its agencies included in short-term investments on balance sheet	$161,685	$159,972	$163,102
State and municipal bonds—			
California Department of Veteran Affairs bond	$ 9,785	$ 10,137	$ 10,540
Washington State G.O. note	9,080	9,110	11,030
Oregon State Veterans' Welfare bond	3,500	3,824	4,067
Other	6,920	6,916	6,906
		$ 29,987	$ 32,543
Common stock—			
Exxon Corporation	670,300	$ 29,764	$ 30,164
General Foods Corporation	606,268	20,573	33,873
Northwest Industries, Inc.	329,400	15,525	16,140
		$ 65,862	$ 80,177
Preferred stock—			
So. California Edison Company	154,100	$ 6,082	$ 5,963
Pacific Gas & Electric Company	316,700	6,078	5,528
Cincinnati Gas & Electric Company	41,400	2,907	2,429
Florida Power & Light Company	25,000	2,500	1,853
Utah Power & Light Company	108,000	2,287	2,450
Houston Lighting Company	30,075	1,790	1,785
ANR Pipeline Company	61,500	1,506	1,207
Public Service Electric & Gas Company	36,650	1,484	1,500
Issued by others	99,940	5,696	5,968
		$ 30,330	$ 28,683

All of the securities listed above were held by Mutual Savings and Loan Association except as indicated below:

Held by Wesco Financial Corporation (registrant)—			
U.S. Government securities	$ 55,535	$54,700	$ 56,171
General Foods Corporation common stock	393,259 shares	12,613	21,973
		$67,313	$ 78,144
Held by Precision Steel Warehouse, Inc. (wholly owned subsidiary of Wesco Financial Corporation)—			
U.S. Government securities	$ 15,750	$14,992	$ 15,939
General Foods Corporation common stock	212,969 shares	7,960	11,900
Northwest Industries, Inc. common stock	175,100 shares	8,242	8,580
		$31,194	$ 36,419
Held by Wes-Fin Service Corp. (wholly owned subsidiary of Mutual Savings and Loan Association)—			
U.S. Government securities	$ 3,500	$ 3,460	$ 3,629
Exxon Corporation common stock	459,900 shares	20,455	20,696
Northwest Industries, Inc. common stock	37,300 shares	1,790	1,827
		$25,705	$ 26,152

WESCO FINANCIAL CORPORATION

SCHEDULE III—CONDENSED FINANCIAL INFORMATION OF REGISTRANT

BALANCE SHEET

(Dollar amounts in thousands)

	December 31, 1984	December 31, 1983
ASSETS		
Cash (including savings accounts at Mutual Savings of $403 and $15,025)	$ 434	$ 15,061
Short-term investments	54,700	—
Common stocks, at cost (market $21,973 and $64,900)	12,613	46,189
Income taxes receivable	—	923
Advance to subsidiary	4,200	4,200
Investment in subsidiaries, at equity	99,019	85,547
Premises and equipment, net	3,069	3,077
Other assets	748	794
	$174,783	$155,791
LIABILITIES AND SHAREHOLDERS' EQUITY		
Notes payable	$ 30,182	$ 30,166
Accounts payable and accrued expenses	506	676
Income taxes payable	456	837
Total liabilities	31,144	31,679
Shareholders' equity:		
Capital stock, $1 par value—authorized 7,500,000 shares; issued 7,119,807 shares	7,120	7,120
Capital surplus resulting from stock dividends	23,319	23,319
Retained earnings—partially restricted	113,200	93,673
Total shareholders' equity	143,639	124,112
	$174,783	$155,791

See notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION

SCHEDULE III—CONDENSED FINANCIAL INFORMATION OF REGISTRANT

STATEMENT OF INCOME AND RETAINED EARNINGS

(Dollar amounts in thousands)

	Years Ended December 31,		
	1984	1983	1982
Revenues—			
Dividends on common stocks	$ 2,208	$ 3,189	$ 3,702
Interest on short-term investments	3,138	—	—
Interest on savings accounts at Mutual Savings	1,048	1,510	590
Rental of office, store and garage premises, net	1,694	1,558	1,406
Dividends from subsidiaries	—	—	1,138
Gain on sales of marketable securities	10,635	218	8,496
Other	30	62	62
	18,753	6,537	15,394
Expenses—			
Interest on notes payable	3,086	3,017	3,028
General and administrative	576	577	559
	3,662	3,594	3,587
Income before items shown below	15,091	2,943	11,807
Income tax provision	(4,907)	(242)	(2,475)
Equity in undistributed earnings of subsidiaries	13,472	7,852	2,170
Net income	23,656	10,553	11,502
Retained earnings—beginning of year	93,673	86,964	79,022
Cash dividends	(4,129)	(3,844)	(3,560)
Retained earnings—end of year	$113,200	$93,673	$86,964

See notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION

SCHEDULE X—SUPPLEMENTARY INCOME STATEMENT INFORMATION

(Dollar amounts in thousands)

The following expenses have been included in the respective statements of income of the consolidated entity and the registrant alone:

	Consolidated		
	Financial	Steel Service	Registrant
1984:			
Maintenance and repairs	$370	$447	$344
Property taxes	123	179	82
Advertising	150	299	—
1983:			
Maintenance and repairs	373	375	345
Property taxes	121	171	77
Advertising	170	306	—
1982:			
Maintenance and repairs	353	333	329
Property taxes	97	165	75
Advertising	164	324	—

MUTUAL SAVINGS AND LOAN ASSOCIATION
(A Wholly Owned Subsidiary of Wesco Financial Corporation)
CONDENSED CONSOLIDATED BALANCE SHEET

(Dollar amounts in thousands)

	December 31, 1984	December 31, 1983
ASSETS		
Cash and short-term investments	$ 92,185	$ 61,987
State and municipal bonds, at cost (market $32,543 and $33,230)	29,987	30,958
Marketable equity securities, at lower of aggregate cost or market:		
Common stocks—		
Owned by Mutual Savings (cost $14,802)	15,201	—
Owned by service subsidiary (cost $22,245 in 1984; market $24,980 in 1983)	22,523	20,186
Preferred stocks owned by Mutual Savings (cost $27,724 in 1984; market $26,236 in 1983)	26,349	27,724
Other marketable securities, at cost:		
Preferred stocks (market $2,334 and $2,416)	2,606	2,606
Loans receivable, principally real estate, yielding 7.63% and 7.48%	95,120	106,831
Income taxes receivable	761	3,585
Real estate held for sale	2,011	4,480
Investment in stock of Federal Home Loan Bank and prepayments to FSLIC secondary reserve	4,283	4,029
Other assets	4,016	3,850
	$295,042	$266,236
LIABILITIES AND SHAREHOLDER'S EQUITY		
Savings accounts	$227,585	$203,284
Advances from Federal Home Loan Bank	—	1,401
Accounts payable and accrued expenses	474	570
Deferred income taxes	5,432	5,576
	233,491	210,831
Shareholder's equity:		
Guarantee stock and additional paid-in capital	100	100
Retained earnings—substantially restricted	62,149	55,305
Net unrealized loss on marketable equity securities	(698)	—
Total shareholder's equity	61,551	55,405
	$295,042	$266,236

See notes to consolidated financial statements of Wesco Financial Corporation.

END