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WESCO FINANCIAL CORP

10-K

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CARD 1 DISCLOSURE INFORMATION GROUP BETHESDA MD 20816 FOR 12/31/85

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

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WESCO FINANCIAL CORPORATION

Annual Report 1985

Form 10-K Annual Report 1985

Headquarters building
of Wesco Financial Corporation
and Mutual Savings and Loan Associati

BOARD OF DIRECTORS

Charles T. Munger
Chairman of the Board, Wesco Financial Corporation and Mutual Savings and Loan Association; President, Wesco Financial Corporation; Chairman of the Board, Blue Chip Stamps (trading stamps and motivation programs, parent of Wesco Financial Corporation); Vice Chairman of the Board, Berkshire Hathaway Inc. (insurance, candy, retailing, manufacturing, newspaper and encyclopedia publishing, parent of Blue Chip Stamps).

William T. Caspers*
Personal investments

Harold R. Dettmann
Vice President, Wesco Financial Corporation; President, Mutual Savings and Loan Association

James N. Gamble*
Investment counselling and trust administration

Elizabeth Caspers Peters
Personal investments

David K. Robinson*
Partner of Hahn & Hahn, attorneys at law

*Audit Committee member

EXECUTIVE OFFICERS OF WESCO FINANCIAL CORPORATION AND MUTUAL SAVINGS AND LOAN ASSOCIATION

Charles T. Munger
Chairman of the Board and President, Wesco; Chairman of the Board, Mutual Savings

Harold R. Dettmann
Vice President, Wesco; President, Mutual Savings

John R. Armetta
Vice President, Wesco; Senior Vice President, Mutual Savings

Philip E. Lynn
Vice President, Wesco; Senior Vice President, Mutual Savings

Robert E. Sahm
Vice President, Wesco

Jeffrey L. Jacobson
Vice President and Chief Financial Officer, Wesco and Mutual Savings

Jeanne Leach
Treasurer, Wesco; Vice President and Controller, Mutual Savings

Dolores Henderson
Secretary, Wesco and Mutual Savings

Robert D. Aston
Senior Vice President, Mutual Savings

Dolly Russo
Senior Vice President and Branch Manager, Mutual Savings

LEGAL COUNSEL

Hahn & Hahn

LISTED ON

American Stock Exchange
Pacific Stock Exchange

TRANSFER AGENTS AND REGISTRARS

Security Pacific National Bank
P.O. Box 3546, Terminal Annex, Los Angeles, California 90051

Security Pacific National Bank
63 Wall Street, 13th Floor, New York, New York 10004

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 1985 decreased to $8,347,000 ($1.17 per share) from $10,060,000 ($1.42 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 $51,541,000 ($7.24 per share) from $23,656,000 ($3.32 per share) in the previous year.

A highly unusual capital gain, of a not-likely-to-recur type, from disposition of General Foods stock caused most of the net income in 1985. The table below gives particulars.

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

	Year Ended			
	December 31, 1985		December 31, 1984	
	Amount	Per Wesco Share	Amount	Per Wesco Share
"Normal" net operating income (loss) of:				
Mutual Savings	$ 3,342	$ .47	$ 3,476	$ .49
Precision Steel businesses	2,010	.28	2,034	.29
Wesco-Financial Insurance business—				
Underwriting	(1,584)	(.22)	—	—
Investment activity	1,225	.17		
	(359)	(.05)		
All other "normal" net operating income[2]	3,354	.47	4,550	.64
	8,347	1.17	10,060	1.42
Fluctuation in market value of GNMA futures contract	1,671	.24	458	.06
Net gains on sales of securities[3]	41,523	5.83	13,138	1.84
Wesco consolidated net income	$51,541	$7.24	$23,656	$3.32

(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 and insurance subsidiaries.

(3) The 1985 figure includes a $34,363,000 ($4.83 per share) gain realized by Wesco on the sale of its General Foods Corporation common stock to Philip Morris Company in connection with the latter's publicly announced tender offer. See "Net Gains on Sales of Securities" below.

This supplementary breakdown of earnings differs somewhat from that used in audited financial statements which follow standard accounting convention. The supplementary breakdown is furnished because it is considered useful to shareholders.

Mutual Savings

Mutual Savings' "normal" net operating income of $3,342,000 in 1985 represented a decrease of 4% from the $3,476,000 figure the previous year.

Separate balance sheets of Mutual Savings at yearend 1984 and 1985 are set forth at the end of this annual report. They show (1) total savings accounts rising to $269 million from $228 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, (4) a loan portfolio (mostly real estate mortgages) of about $83 million at the end of 1985, down 12% from the $95 million at the end of 1984, and (5) favorable effects of securities gains and other unusual gains and fluctuations, which caused net worth to decline only $4 million in 1985 despite payment of a dividend of $14 million to the parent corporation.

The loan portfolio at the end of 1985, although containing almost no risk of loss from defaults, bore a fixed average interest rate of only 7.60%, 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. However, as the loan payoff pace intensified and interest rates declined sharply in 1985, the unrealized depreciation in the loan portfolio became approximately offset by unrealized appreciation in Mutual Savings' interest-bearing securities and preferred stocks.

As pointed out in footnote 13 to the accompanying financial statements, the book value of Wesco's equity in Mutual Savings ($57.6 million at December 31, 1985) overstates the amount realizable, after taxes, from sale or liquidation at book value. If all Mutual Savings' assets, net of liabilities, were to be sold, even pursuant to a plan of complete liquidation, for the $57.6 million in book value reported under applicable accounting convention, the parent corporation would receive much less than $57.6 million after substantial income taxation imposed because about $47 million of what is designated shareholders' equity for accounting purposes is considered bad debt reserves for most tax purposes.

There is, however, a buried plus value in Mutual Savings. The foreclosed property on hand (mostly 22 largely oceanfront acres in Santa Barbara) has become worth over a long holding period much more than its $1.5 million balance sheet carrying cost. Reasonable, community-sensitive development of this property has been delayed over 10 years in the course of administration of land-use laws. But we are optimistic that an end to the delay is near and that the Santa Barbara and Montecito communities will be very pleased with the development now likely to go forward. This development will contain 32 houses interspersed with large open areas. Mutual Savings plans to make the development first rate in every respect, and unique in the quality of its landscaping.

Balancing all merits and demerits, Mutual Savings, as it has been managed under present conditions by the writer and others, is no jewel of a business from the shareholders' point of view. Mutual Savings' good points are: (1) high asset quality and sound balance sheet; (2) a maturity match of interest-bearing assets and liabilities which makes risk of insolvency near zero, whatever happens to interest rates; and (3) a deserved reputation for high quality service to account holders, achieved at below-average cost to the institution in an efficient one-large-office operation, as distinguished from a many-small-branch-offices operation. Mutual Savings' bad points are: (1) all recent growth in savings accounts, considered on an incremental effects basis, has been loss business because interest and other costs incurred exceed income obtained by employing proceeds in short-term interest-bearing assets; (2) a burdensome position under the FSLIC account-insurance system causes payments of ever-higher amounts into the system to help bail out more venturesome savings and loan associations which become insolvent, with the payments being required despite the fact that Mutual Savings imposes almost no risk on FSLIC; (3) "normal" net operating income is below an acceptable rate of return on present book value of shareholders' equity, with such return reaching an acceptable level over recent years only with help from securities gains and other unusual items; (4) it would not be easy to leave the savings and loan business, should this course of action ever be desired, without a large income tax burden of a type not applied to corporations other than savings and loan associations; (5) the regulatory structure of the savings and loan business creates a competitive situation in which it is hard to make respectable profits through careful operations; and (6) management has not yet found an acceptable remedy for any of the previously listed bad points, despite years of trying.

Moreover, comparisons of post-1984 financial results for Mutual Savings with results for many other and more typical savings and loan associations in California leave Mutual Savings looking inferior, to put it mildly. As interest rates went down these other associations, which have greater financial leverage and operated less fearfully than Mutual Savings during former high-interest periods, came to have loan and investment portfolios which (1) now are worth more on average than book value and (2) now produce a high return on book value of shareholders' equity, after deduction of operating expenses and interest to account holders at present rates. Any Wesco shareholder who thinks Mutual Savings has any expertise in predicting and profiting from interest rate changes can look at the 1985 record and despair.

Despite the fact that some other savings and loan associations did much better after 1984 than Mutual Savings, and are now much better poised to report good figures for 1986, we plan to continue operating only in ways acceptable in our own judgment, anticipating as a consequence widely fluctuating and sometimes inadequate returns. In the future, however, Mutual Savings will make and purchase more loans. Now that Mutual Savings' old mortgage loans have declined in amount and increased in market value (the market value increase being caused both by a decline in generally prevailing interest rates and by a shortening of remaining loan life), new loans will be added as seems wise, with a target that 60% of assets be in housing-related loans. The first new direct loan in some time, an adjustable rate mortgage with no cap on future interest rate changes but with an extremely low "spread" for the lender, will shortly be closed. We are not at all excited by our prospects as we now make housing loans of this type, but we wish to get some renewal of direct mortgage lending under way.

With assets not employed in direct real-estate lending, Mutual Savings continues not only to make payments to FSLIC far in excess of fair charges for risks imposed on FSLIC but also to employ a large part of total assets in short-term loans to the Federal Home Loan Bank. These practices are pro-social but will continue to reduce profits.

Mutual Savings also continues to support the Federal Home Loan Bank Board in its efforts to change the present rules of the savings and loan business to augment average soundness of FSLIC-insured associations. We retain our opinion that the present rules, despite some improvement in 1985 through wise efforts of the Federal Home Loan Bank Board, are unsound, from the country's point of view. Too much latitude is allowed financial "swingers" to grow as they gamble, through use of account guarantees from FSLIC, an agency of the U.S. Government, while they offer whatever it takes in interest rates to attract more accounts.

With money being the ultimate fungible commodity, it seems to us that the rules create a super-competitive, commodity-type business, in which (1) economic law probably destines most careful associations, like other fungible-commodity dealers, to realize very modest returns on shareholders' equity over extended time periods, yet (2) good financial results can nonetheless usually be reported in each near-term period by managers-in-charge through aggressive deposit-expanding, lending and investing measures which increase risk, while (3) the importance and rewards of managers, who usually have little downside risk as owners, are tied mostly to institutional size and recently reported numbers. With managers mostly being non-owners, a sort of Gresham's law of competitive-yet-deposit-insured banking, "bad loans drive out good," tends to work with extra force as managers fear being left out of whatever activity allows competing managers to report high profits while bidding high for deposits. We see no reason for assuming that ethical, intelligent managers in the savings and loan industry are immune from effects similar to those which caused similar managers of all major U.S. banks to place significant portions of assets in now-regretted foreign loans, rather than stand apart from the crowd. If our diagnosis is correct, a lot of serious trouble lies ahead (perhaps far ahead) for U.S. savings and loan associations.

While present rules and practices have a positive side in causing satisfaction of almost 100% of demand for those housing loans which are sound at the prevailing interest rate, this accomplishment is accompanied by much unsound housing and other lending and by much unsound investment in "junk bonds" and other assets unsuitable for highly leveraged, federally insured, deposit-taking institutions. The system design in place would probably be a flunking design in an engineering course, where the emphasis would be on preserving the integrity of an essential system by a margin of safety, by being content with rules which (1) caused satisfaction of, say, only 95% of requests for sound credit extension and (2) forced more conservative conduct on banks and savings and loan associations.

The present design, we think, would probably also be a flunking design in a surgery course, where the wise practice is to remove some healthy cells along with cancerous cells, based on margin-of-safety principles. We hope we are wrong about the present design of the savings and loan system, but we fear increased, widespread adversity, ultimately reaching housing borrowers and would-be housing borrowers, whose interests we consider important. Any such adversity would probably be followed by changes in the rules. No doubt, our judgment as to the probable temporary nature of present savings and loan industry structure and practices has helped deter us from direct lending of a conventional sort which otherwise would have occurred. Our attitude, right or wrong, during recent tumultuous changes in the savings and loan industry, has been roughly that of the French grandfather who replied when asked what he did in the great revolution: "I got through." We also think something good could eventually happen to Mutual Savings because future trouble in the savings and loan business may create opportunities worth seizing.

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, the company 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 $2,010,000 to "normal" net operating income in 1985, down 1% compared with $2,034,000 in 1984. Such a modest decrease in 1985 profit was achieved in spite of decreased sales (down 7% to $51,124,000).

Under the skilled 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.

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 $9,140,000 to 1985 sales at a profit margin 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 available liquid assets.

Wesco-Financial Insurance Company

A new business was added to the Wesco group in 1985, in co-venture with Wesco's 80% owner and ultimate parent corporation, Berkshire Hathaway Inc.

With the enthusiastic approval of all Wesco's directors, including substantial Wesco shareholders in the Peters and Caspers families, without whose approval such action would not have been taken, Wesco invested $45,000,000 in cash equivalents in a newly organized, wholly owned, Nebraska-chartered insurance company, Wesco-Financial Insurance Company ("Wes-FIC").

The new subsidiary, Wes-FIC, then reinsured, through another Berkshire Hathaway insurance company subsidiary as intermediary-without-profit, 2% of the entire book of insurance business of the long-established Fireman's Fund Corp. (listed on the NYSE).

Wes-FIC thereby assumed the benefits and burdens of Fireman's Fund's prices, costs and losses under a contract covering all insurance premiums earned by Fireman's Fund during a four-year period commencing September 1, 1985. The arrangement puts Wes-FIC in almost exactly the position it would have been in if it, instead of Fireman's Fund, had directly written 2% of the business. Differences in results should occur only from the investment side of insurance, as Wes-FIC, instead of Fireman's Fund, invests funds from "float" generated. Wes-FIC's share of premiums earned in 1986 is expected to be over $60 million.

Wes-FIC's separate financial statements, covering the brief period of its existence, September 1, 1985, to December 31, 1985, are included on pages 29 and 30 of this Annual Report, and show that Wes-FIC experienced a small 1985 reduction in net worth, from $45,000,000 to $44,676,000.

We do not consider this four-month result to have significant predictive value with respect to the future. The price of insurance is rising, with price increases not yet fully reflected in 1985 numbers. Moreover, the financial statements are of questionable accuracy and could be wrong in either direction. It is in the nature of even the finest casualty insurance businesses that in keeping their accounts they must estimate and deduct all future costs and losses from premiums already earned. Uncertainties inherent in this undertaking make financial statements more mere "best honest guesses" than is typically the case with accounts of non-insurance-writing corporations. And the reinsurance portion of the casualty insurance business, because it contains one or more extra links in the loss-reporting chain, usually creates more accounting uncertainty than the non-reinsurance portion. Finally, Wes-FIC's initial financial statements have a disadvantage in that the period covered is short, making any use of the reported past cost-price ratio extra dubious as an indicator of any probable future cost-price ratio, due to the small size of the sample forming a base for projection.

It is entirely too soon to forecast future results for Wes-FIC, but Wesco hopes for: (1) a reasonable return on its investment over the four years of the Fireman's Fund reinsurance contract, and (2) possible future reinsurance contracts with other insurers.

Wesco has high regard for John Byrne, newly appointed CEO and also a large shareholder and stock-option holder of Fireman's Fund. Mr. Byrne was an outstanding insurance company manager in his previous position as CEO of GEICO CORPORATION (38%-owned, but not controlled, by Berkshire Hathaway), which improved enormously during his stewardship. Fireman's Fund's insurance business is intrinsically more cyclical and less-advantaged than GEICO's core insurance business, which has lower distribution costs from a different, "direct-writing" distribution system. Thus Fireman's Fund's business will almost surely be much more difficult to improve permanently than was the case at GEICO. However, Mr. Byrne and other Fireman's Fund executives know all this very well, and, with improvement less spectacular than previous improvement at GEICO, Fireman's Fund and Wes-FIC could both prosper.

Industry-wide conditions, as well as managerial excellence, affect Wes-FIC's prospects under the reinsurance contract with Fireman's Fund. Large premium increases now going into effect throughout the casualty insurance business could provide some welcome tailwind effects, instead of the headwind effects of the period just ended, which was one of the worst in history.

We are pleased with our relationship with Fireman's Fund, which has a long and distinguished record, going all the way back to superb performance after the great San Francisco earthquake and fire, and which is affiliated with the even longer established American Express Company, one of the premier corporations in the United States.

However, Wesco's optimism about quality of Fireman's Fund, quality of this reinsurance contract, and possible short-term, industry-wide cyclical improvement, is tempered by a larger and longer view of the reinsurance business. That business has the defect of being too attractive-looking to new entrants for its own good and therefore will always tend to be more or less the opposite of, say, the old business of gathering and rendering dead horses, which tended to contain few and prosperous participants.

Troubles, losses, and insolvencies can come fast as the apparent attractions of the reinsurance business, including its seductive receive-pay-in-advance aspects, lure new entrants and encourage expansions by old occupants. The business was a disaster area in recent years, adversely affected by prices which would have been too low in a stable world, plus inflation, new judicial notions tending to augment insurance coverage beyond limits contemplated when policies were issued, and not-minor degradation of commercial behavior.

No doubt recent commercial behavior degradation, particularly noticeable in the reinsurance business on both sides of the purchase counter, was accelerated by general hardship, demonstrating once again the wisdom of Poor Richard's Almanac: "It is hard for an empty sack to stand upright."

Insurance company subsidiaries of Wesco's parent corporation, Berkshire Hathaway, long active in reinsurance, did continue proper commercial behavior during the recent period of industry-wide problems, but financial results from reinsurance were terrible. Thus Wesco shareholders are being led not only into an extra-hazardous place but also by people who met severe reverses on the last trip.

Is there any reasonable hope for Wesco shareholders that its reinsurance business, whatever its short-term merits, will provide an advantageous long-term journey? Yes, one reason for long-term optimism is present. With recent defaults by reinsurers causing everyone to worry more about quality in promisors, Wes-FIC and Berkshire Hathaway expect that their old-fashioned, engineering-type attitudes and financial practices will help create for Wes-FIC an unusual, commercially-useful reputation for issuing trustworthy promises in one or more markets or submarkets wherein most buyers will accept nothing less. Thus, the absence of federal insurance for reinsurance liabilities may create for Wes-FIC a reputation-based competitive advantage which is denied to Mutual Savings by FSLIC's support of all Mutual Savings' competitors through insuring their accounts.

All Other "Normal" Net Operating Income

All other "normal" net operating income, net of interest paid and general corporate expenses, decreased to $3,354,000 in 1985 from $4,550,000 in 1984. Sources were (1) rents ($2,219,000 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 $41,523,000 in 1985 from $13,138,000 in 1984.

The 1985 figure includes a big after-tax gain ($34,363,000) from sale of General Foods stock to Philip Morris Company. This gain contained a large amount of windfall profit. When Wesco made its investment in General Foods stock several years ago, because General Foods' executives seemed sensible and the stock was available in the market at a conservative price relative to its value as a share of ownership in a presumably ever-continuing independent entity, it was unprecedented and virtually inconceivable that a corporation the size of General Foods would ever be "bear-hugged" into selling out at an immense premium over the then prevailing market price for its stock. But that is what happened, wholly unpredicted by Wesco, in 1985 as old taboos eroded and the great American takeover game swept into new areas.

Bowery Savings Bank

In 1985 Wesco, in another co-venture with its parent corporation, approved by Wesco's directors in the same manner as the Wes-FIC co-venture, joined a group which invested $100,000,000 cash in a newly organized, New York-chartered savings bank. The new bank then took over the name, assets and liabilities of the insolvent Bowery Savings Bank in the city of New York. The takeover received (1) much needed assistance from FDIC, the federal agency, akin to FSLIC, which insures deposits in banks, and (2) the blessing of New York bank regulators. Wesco invested $9,000,000, other Berkshire Hathaway subsidiaries invested $12,384,000, and other unrelated investors invested the balance of the $100,000,000.

The terms of the FDIC assistance, which include income-assistance payments over many years to the newly organized bank, are extremely complex but can be fairly summarized as far from adequate to assure that the investors will make a profit. This is as it should be when $100 million buys a highly-leveraged residual equity position in a $5 billion bank, albeit one with many sick assets.

Any minority-position investment with such extreme financial leverage (in effect buying with a 2% down payment), involving a troubled company in a demanding environment, can fairly be called a venture-capital type investment for Wesco. In our judgment, the prospect for gain justified the risk of loss. The investment involves a small portion (about 5%) of Wesco's consolidated net worth. We consider it financially conservative to risk 3½% of Wesco's net worth, which is roughly the after-tax exposure involved, if we believe a hundred similar bets would, in aggregate, be almost sure to work out successfully.

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 slow pace of acquisition of additional businesses because few are found available, despite constant search, at prices deemed rational from the standpoint of Wesco shareholders.

As indicated in Note 3 to the accompanying financial statements, the aggregate market value of Wesco's marketable equity securities was higher than their aggregate cost at December 31, 1985 by about $5 million, down sharply from about $13 million one year earlier.

Wesco's Pasadena real estate, a full block (containing (1) about 125,000 first class net rentable square feet, including Mutual Savings' space, in a modern office building, plus (2) an additional net rentable 34,000 square feet of economically marginal space in old buildings requiring expensive improvement), has a market value substantially in excess of carrying value, demonstrated by (1) mortgage debt ($5,023,000 at 9.25% fixed) against this real estate now exceeding its depreciated carrying value ($3,158,000) in Wesco's balance sheet at December 31, 1985, and (2) substantial current net cash flow (about $1 million per year) to Wesco after debt service on the mortgage. The modern office building is 96% rented, despite a glut of vacant office space in Pasadena. We charge just-below-standard rents and run the building as a sort of first-class club for tenants we admire. With these practices, a prime location and superior parking facilities, we anticipate future increases in cash flow, but at no better rate than the rate of inflation.

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, investments, both those in the savings and loan and reinsurance subsidiaries and those held temporarily elsewhere pending sale to fund business extension, tend to be concentrated in very few places. Through this practice of concentration of investments, 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 21% in 1983-85, was dependent to a very large extent on securities gains, irregular by nature. The recent ratio is almost certain to decline, quite probably very sharply. Neither possible future acquisitions of other businesses nor possible future securities gains appear likely to cause the recent ratio to continue. The business acquisition game is now crowded with optimistic players who usually force prices for low-leverage acquirers like Wesco to levels where return-on-investment prospects are modest. And, as discussed earlier, the great contribution of 1985 securities gains to Wesco's recent return on shareholders' equity contained a big fluke element. Such fluke gain, rare in any event, tends to come to an investor like Wesco mostly as an unanticipated by-product of an obviously sound investment which does not require any fluke to work out well. Because securities generally traded lower several years ago than they do now, relative to the intrinsic values of the businesses represented by the securities, creating more obviously sound investments then than now, and because prospects for above-average returns tend to go down as assets managed go up, it is now easy to predict less desirable future results. It is also easy for any sophisticated Wesco shareholder, reviewing Wesco marketable securities disclosed in the 1985 Annual Report, to diagnose (correctly) that the decision-makers are dry of good investment ideas.

Wesco is trying more to profit from always remembering the obvious than from grasping the esoteric (including much modern "strategic planning" and "portfolio theory"). Such an approach, while it has worked fairly well on average in the past and will probably work fairly well over the long-term future, is bound to encounter periods of dullness and disadvantage as it limits action. Moreover, the approach is being applied to no great base position. Wesco is sort of scrambling through the years without owning a single business, even a small one, with enough commercial advantage in place to pretty well assure high future returns on its capital. In contrast, Berkshire Hathaway, Wesco's parent corporation, owns three such high-return businesses.

On January 23, 1986, Wesco increased its regular quarterly dividend from 15½ cents per share to 16½ cents per share, payable March 6, 1986, to shareholders of record as of the close of business on February 17, 1986.

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 13, 1986

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, 1985 | Commission file number 1-4720

WESCO FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	95-2109453 (I.R.S. Employer Identification No.)
315 East Colorado Boulevard, Pasadena, California (Address of principal executive offices)	91101-1954 (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 6, 1986 was: $56,897,368.

The number of shares outstanding of the registrant's Capital Stock as of March 6, 1986 was: 7,119,807.

DOCUMENTS INCORPORATED BY REFERENCE

Title of Document	Parts of Form 10-K
Proxy Statement for 1986 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, conducted by wholly owned subsidiaries, are the savings and loan business, through Mutual Savings and Loan Association ("Mutual Savings"), which was incorporated in California in 1925, the steel service center business, through Precision Steel Warehouse, Inc. ("Precision Steel"), which was begun in 1940 and acquired by Wesco in 1979, and the property and casualty insurance business, through Wesco-Financial Insurance Company ("Wes-FIC"), which was incorporated in Nebraska in 1985. 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 (a) the savings and loan business, (b) the property and casualty insurance business, (c) operation of a business block in Pasadena, California, and (d) investments, principally 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 been and are 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 any 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 will be completely eliminated by April 1, 1986. 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.

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 while pondering a sound operating plan that would provide a socially constructive service while operating with acceptable profits accompanied by an acceptable level of risk. 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. Mutual Savings has not engaged in direct real estate lending to a significant extent since that time.

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 approximately $2,900,000.

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 75th among California's savings and loan associations in assets at the end of 1985. 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 (7.6% per annum at the end of 1985) among all associations in the United States. This remaining portfolio, carried on Mutual Savings' books at the end of 1985 at about $83,000,000, is worth somewhat 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 preferred stocks. These assets currently produce a tax-equivalent yield believed to be somewhat below that prevailing on the mortgage portfolio of the typical association, which operated less fearfully than Mutual Savings during former high-interest periods.

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. In the 1984 annual report it was reported that Mutual Savings had, in April 1984, purchased a futures contract and agreed to buy in 1986 $30,000,000 face amount of real estate loans, backed by GNMA certificates, at a price of approximately $19,000,000. As the delivery date approached and interest rates declined, Mutual Savings closed out the futures contract in September 1985, exercising business judgment under changed conditions. Gain recorded from holding and closing out the contract amounted to $458,000 and $1,671,000, after income taxes, in 1984 and 1985, respectively.

Mutual Savings has recently decided to re-enter real estate lending, and is in process of marketing a fully adjustable-rate mortgage loan, with no cap on future interest rate changes or on changes in borrower payments. These loans are expected to yield a substandard "spread" (less than 2%) above the rate quoted on 1 year U.S. Treasury bills. Management is hopeful that Mutual Savings' portfolio of real estate loans eventually will grow substantially, with the target that 60% of assets will ultimately be in high-quality housing-related loans.

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. These securities were sold during 1985, and, at 1985 yearend, Mutual Savings had not yet reinvested in common stocks.

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.

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, 1985, Wes-Fin had invested the sum of $19,943,000 in common stocks under this authority.

During 1985, Mutual Savings, excluding its service subsidiary, sustained a pre-tax operating loss before gains on GNMA futures contracts and sales of securities. 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.

In August 1985, Wesco formed a wholly owned subsidiary, Wesco-Financial Insurance Company ("Wes-FIC"), to engage in the property and casualty insurance and reinsurance business. Wesco contributed, as initial capital, $45,000,000 in cash and cash-equivalents to Wes-FIC in September 1985.

Wes-FIC then reinsured, through a Berkshire Hathaway insurance company subsidiary, National Indemnity Company ("NICO"), as intermediary-without-profit, 2% of the entire book of insurance business of the long-established Fireman's Fund Insurance Companies. Wes-FIC thus assumed the benefits and burdens of Fireman's Fund's prices, costs and losses under a contract covering all insurance premiums earned by Fireman's Fund during a four-year period commencing September 1, 1985. The arrangement puts Wes-FIC in virtually the same position it would have been in if it, instead of Fireman's Fund, had directly written the business reinsured. Differences in results should occur only from the investment side of insurance, as Wes-FIC, instead of Fireman's Fund, invests funds from "float" generated. Wes-FIC's share of premiums earned in 1986 is expected to be over $60,000,000.

Wesco, while it seeks suitable additional businesses to acquire, and expansion of its existing operations, invests in marketable common stocks of unaffiliated companies. (See Note 3 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.

Wesco, as a savings and loan and insurance holding company, Mutual Savings, as a savings and loan association, and Wes-FIC, as an insurance company, 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.

Approximately 60 full-time employees are engaged in the savings and loan business and other financial segment activities. Wes-FIC is operated by personnel employed by Berkshire and NICO; it has no employees of its own.

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. Competitive pressure is intensified by imports and by a tendency of domestic manufacturers to substitute less costly components for parts traditionally made of steel.

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 their area of the economy. These businesses are not dependent on a few large customers. Steel service backlog orders decreased to approximately $4,325,000 as of December 31, 1985 from approximately $5,350,000 as of December 31, 1984.

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 125,000 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 and may be extended under two five-year options.

Wesco-Financial Insurance Company uses the headquarters office of NICO, a subsidiary of Berkshire Hathaway Inc., its ultimate parent, in Omaha, Nebraska, as its place of business.

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.

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 are expected to result in material 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 1985.

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 1985 and 1984, as well as cash dividends paid by Wesco on each outstanding share:

	1985				1984		
	Sales Price		Dividends		Sales Price		Dividends
Quarter Ended	High	Low	Paid	Quarter Ended	High	Low	Paid
March 31	$29	$21⅜	$0.155	March 31	$19½	$16¼	$0.145
June 30	29¼	24⅞	0.155	June 30	19⅛	16½	0.145
September 30	29⅛	27⅜	0.155	September 30	19⅛	16⅜	0.145
December 31	41¼	29¼	0.155	December 31	22⅝	17¾	0.145
			$0.62				$0.58

There were approximately 1,100 shareholders of record of Wesco's common stock as of the close of business on February 17, 1986.

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 Wesco's audited 1985 consolidated financial statements appearing elsewhere in this report. (Dollar amounts are in thousands except for amounts per share.)

	Year Ended December 31,				
	1985	1984	1983	1982	1981
Financial:					
Revenues—					
Interest on loans	$ 6,794	$ 7,711	$ 8,567	$ 9,786	$ 12,211
Interest on investments	24,651	17,170	9,294	8,975	8,597
Dividends on common and preferred stocks	6,944	7,765	9,025	8,298	7,904
Insurance premiums earned	20,412	—	—	—	—
Fluctuation in market value of GNMA futures contract	2,803	938	—	—	—
Gain on sale of marketable securities	62,895	19,360	3,025	9,998	2,643
Other	2,033	1,952	1,787	2,204	1,566
	126,532	54,896	31,698	39,261	32,921
Expenses—					
Interest on savings accounts	25,191	20,940	16,870	15,985	15,970
Insurance losses and expenses	23,008	—	—	—	—
Interest on notes payable	3,035	3,103	4,673	6,199	6,778
General and administrative	4,031	3,347	3,452	3,355	3,611
Loss on sale of loans	—	—	—	4,761	147
	55,265	27,390	24,995	30,300	26,506
Income before income taxes	71,267	27,506	6,703	8,961	6,415
Income tax (provision) benefit	(21,736)	(5,884)	2,228	2,214	1,417
Net income—financial	49,531	21,622	8,931	11,175	7,832
Steel service:					
Revenues—					
Sales	51,124	55,098	46,074	37,293	46,521
Other	181	207	191	189	465
	51,305	55,305	46,265	37,482	46,986
Costs and expenses—					
Cost of products sold	40,914	44,830	37,220	31,426	37,419
Selling, general and administrative expenses	6,600	6,501	5,936	5,492	6,018
	47,514	51,331	43,156	36,918	43,437
Income before income taxes	3,791	3,974	3,109	564	3,549
Income tax provision	(1,781)	(1,940)	(1,487)	(237)	(1,602)
Net income—steel service	2,010	2,034	1,622	327	1,947
Net income—consolidated	$ 51,541	$ 23,656	$ 10,553	$ 11,502	$ 9,779
Amounts per share:					
Net income—consolidated	$7.24	$3.32	$1.48	$1.62	$1.37
Cash dividends	$ .62	$ .58	$ .54	$ .50	$ .46

	December 31,				
	1985	1984	1983	1982	1981
Financial assets:					
Cash and short-term investments	$328,109	$163,348	$ 69,262	$ 57,563	$ 31,201
Common and preferred stocks and state and municipal bonds	97,605	126,179	142,427	119,845	123,755
Loans receivable	83,472	95,172	106,886	123,541	149,656
Other assets	34,163	14,123	18,771	16,480	14,137
	543,349	398,822	337,346	317,429	318,749
Steel service assets	18,608	18,181	17,685	15,337	18,285
Total assets	$561,957	$417,003	$355,031	$332,766	$337,034
Financial liabilities:					
Savings accounts	$269,047	$227,087	$188,195	$152,489	$149,168
Unearned insurance premiums	26,326	—	—	—	—
Unpaid losses and loss adjustment expenses of insurance subsidiary	16,111	—	—	—	—
Notes payable	30,023	30,182	31,567	52,623	68,424
Other liabilities	23,003	10,850	5,907	6,394	5,810
	364,510	268,119	225,669	211,506	223,402
Steel service liabilities	6,646	5,245	5,250	3,857	4,171
Total liabilities	$371,156	$273,364	$230,919	$215,363	$227,573
Shareholders' equity	$190,801	$143,639	$124,112	$117,403	$109,461
Per share	$26.80	$20.17	$17.43	$16.49	$15.37

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"), at the balance sheet of its newly-formed Wesco-Financial Insurance Company ("Wes-FIC") subsidiary, appearing in Note 2 to the accompanying consolidated financial statements, 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) competitive interest rates on other types of accounts. Mutual Savings' unusually high net worth (21 percent of savings accounts at 1985 yearend) has also enabled it to attract and retain savings deposits, as failures and near-failures of other savings and loan associations have drawn much press coverage.

Noteworthy occurrences in 1985 were (1) sales of marketable securities resulting in net gains of $41,523,000 after income taxes, (2) the formation of Wesco-Financial Insurance Company in co-venture with Wesco's 80% owner and ultimate parent, Berkshire Hathaway Inc. (Wesco capitalized Wes-FIC with an initial infusion of $45,000,000 in cash and cash-equivalents in September—see Item 1, Business), and (3) the further decline, about 12%, to $83,425,000, of Mutual Savings' real estate loan portfolio due to its continued lending inactivity.

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, or "gap," between interest-sensitive liabilities and interest-sensitive assets. Federal Home Loan Bank Board policies have recently required that savings and loan associations monitor this gap and restructure maturities of assets and liabilities towards a reduction of interest rate risk. The table below sets forth the major balance sheet categories and dollar amounts of items for Mutual Savings and its consolidated subsidiary as of 1985 yearend which are rate sensitive, and the resulting net gaps as of 1985 and 1984 yearends:

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**
Rate-sensitive assets—						
Cash and short-term investments	$ 157,766	$ 157,766	$ 157,766	$ 157,766	$157,766	$157,766
State and municipal bonds	50	3,835	4,435	4,535	21,660	22,608
Common and preferred stocks	—	—	—	—	—	55,595
Loans receivable**	6,000	12,000	30,000	43,000	68,000	83,425
Total	163,816	173,601	192,201	205,301	247,426	319,394
Rate-sensitive liabilities— Savings accounts	182,131	229,958	265,397	269,274	269,313	269,313
Net gap at— December 31, 1985	$ (18,315)	$ (56,357)	$ (73,196)	$ (63,973)	$ (21,887)	$ 50,081
December 31, 1984	$ (72,887)	$ (90,679)	$ (91,132)	$ (76,114)	$ (30,745)	$ 56,386

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

**Amounts subject to repricing in each period have been estimated inasmuch as they include prepayments as well as normal principal amortization.

The gap analysis demonstrates possibly temporary success in the ongoing restructuring of Mutual Savings' operations, begun in the late 1970s, in order to reduce exposure to interest rate risk and inflation rates (see Item 1, Business). As now restructured, Mutual Savings, and, thus, Wesco's financial segment, are better poised to withstand sharp interest rate increases than in prior years. Mutual Savings is in process of re-entering the real estate lending market, offering adjustable rate mortgage loans with low "spread" over cost of funds and no cap on future interest rate changes. Management is hopeful that these new fully-adjustable rate loans will help Mutual Savings obtain a loan portfolio approximating 60% of its assets, with aggregate interest rate risk at an endurable level.

Mutual Savings is believed to have one of the lowest loan delinquency rates of any savings and loan association due to the seasoned nature of its loan portfolio. At 1985 yearend, monthly payments were past due over 60 days on $124,000 principal balance of such loans.

Wesco is believed to have adequate capital resources for all anticipated operational needs.

RESULTS OF OPERATIONS

Financial Segment

The last several years have seen dramatic, sometimes 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 on securities transactions have increased in importance in Wesco's financial net income. In September 1985, a new business, Wesco-Financial Insurance Company ("Wes-FIC"), was added in co-venture with Wesco's ultimate parent, Berkshire Hathaway Inc. (See Item 1, Business, for further discussion of the changes in the savings and loan 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 indicates the contribution to financial net income from the operations comprising the financial segment, and demonstrates the prevalence and effect on net income of large, unusual items in recent years (amounts are in thousands of dollars, all after income tax effect):

	1985	1984	1983	1982	1981
"Normal" net operating income (loss) of:					
Mutual Savings	$ 3,342	$ 3,476	$ 3,046	$ 3,482	$ 3,457
Wes-FIC	(359)	—	—	—	—
Other operations*	3,354	4,550	3,839	3,412	2,706
	6,337	8,026	6,885	6,894	6,163
Unusual items:					
Gain on sale of marketable securities	41,523	13,138	2,046	6,706	1,669
Fluctuation in market value of GNMA futures contract	1,671	458	—	—	—
Loss on sale of GNMA-backed real estate loans	—	—	—	(2,425)	—
	43,194	13,596	2,046	4,281	1,669
Financial net income, as reported in statements of income	$49,531	$21,622	$ 8,931	$11,175	$ 7,832

*Reflects net commercial real estate rental income, plus interest and dividend income from marketable securities held outside the savings and loan and insurance businesses, from the sum of which is deducted interest and other corporate expenses.

Mutual Savings' consolidated "normal" net operating income has remained relatively unchanged in each of the years presented in the foregoing table, despite significant fluctuations in interest rates. Such operating income has resulted in large part from income tax benefits available to Mutual Savings because of interest income on state and municipal bonds and dividend income on preferred and common stocks, taxed at very favorable corporate rates. Following is a summary of the components of Mutual Savings' consolidated "normal" net operating income (in thousands of dollars):

	1985	1984	1983	1982	1981
Revenues—					
Interest on loans and short-term investments and miscellaneous other revenues	$20,172	$17,572	$14,225	$15,948	$19,002
Dividends on common and preferred stocks	5,455	4,735	4,872	3,686	3,603
Interest on state and municipal bonds	3,220	3,643	3,643	3,604	2,340
	28,847	25,950	22,740	23,238	24,945
Expenses—					
Interest on savings accounts and borrowings, and operating expenses	29,028	25,431	23,539	23,097	23,340
Income (loss) before income tax benefit	(181)	519	(799)	141	1,605
Income tax benefit relating thereto	3,523	2,957	3,845	3,341	1,852
	$ 3,342	$ 3,476	$ 3,046	$ 3,482	$ 3,457

Mutual Savings' costs and expenses have increased in each of the past several years principally as a result of an increase in interest expense on savings accounts, which increase has resulted almost entirely from the growth in savings balances. On an incremental-effects basis such 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. Only the interest on state and municipal bonds and dividends on preferred and common stocks, taxed at favorable rates, have enabled Mutual Savings to report a positive rate spread in recent years. Details are set forth in the following table.

	1985	1984	1983
Yield on loans	7.60%	7.63%	7.48%
Yield on investments*	12.26	14.44	15.01
Combined yield on loans and investments	10.94	11.78	11.43
Cost of savings	(9.81)	(10.30)	(9.97)
Cost of borrowings	—	—	(8.93)
Combined cost of savings and borrowings	(9.81)	(10.30)	(9.88)
Rate spread**	1.13	1.48	1.55

*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.

**The difference between the combined yield on loans and investments and the combined cost of savings and borrowings.

Mutual Savings has little interest rate risk, but also, little rate spread. Such is not typical for many other savings and loan associations, who have continued their long-term lending practices and are currently reporting record earnings and widening rate spreads, resulting mainly from the recent decline in the cost of savings. Although Mutual Savings expects to continue to maintain a positive rate spread, the future of interest rates remains uncertain.

Wesco entered into the property and casualty insurance business in 1985. (See Item 1, Business, for further information on Wesco-Financial Insurance Company—"Wes-FIC.") The separate financial statements of Wes-FIC, covering the four months of its operations, are included in Note 2 to the consolidated financial statements, and show that Wes-FIC sustained a net loss of $359,000 during the period. This four-month result is not considered to have significant predictive value. The liabilities reflected for unpaid losses and loss adjustment expenses of this business are based in large part upon estimates and, therefore, are subject to estimation error. A degree of inaccuracy of as little as 5% in such estimated liabilities would affect Wes-FIC's 1985 results of operations by approximately $450,000, after income taxes. Management believes that a 95% degree of accuracy in the aforementioned stated liabilities, as determined by subsequent events, would indicate a relatively high state of accuracy.

Normal net income from other financial operations (excluding savings and loan and insurance operations), summarized on page 19, decreased to $3,354,000 in 1985 from $4,550,000 in the prior year, principally the result of a decline in yield on short-term investments; the amount invested increased during the year. The increase in this category of net operating income in 1984 over the comparable amount of $3,839,000 for 1983 was attributable mainly to an increase in interest and dividend income as a result of an increase in short-term investments and common stocks during 1984; the yield on such investments also increased.

The securities gains realized in 1985 by Wesco and its subsidiaries include an unusually large amount, $34,363,000 after income taxes, realized from sale of General Foods stock to Philip Morris Company in connection with the latter's tender offer at a large premium over the then-prevailing market price of General Foods' stock. Realized securities gains fluctuate from year to year, but management does not expect Wesco's annual gains in the foreseeable future even to approach their 1985 level. Wesco's history supports such expectation. Wesco has never before realized investment gains of such magnitude in any annual period.

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. Fluctuations in the amounts of and proportion that these investment income components bear to total pre-tax income have resulted in tax provisions and benefits expressed as percentages of pre-tax income, as follows: tax provisions of 30.5% in 1985 and 21.4% in 1984; 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 significant 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 declined approximately 7% in 1985 as a result of a combination of factors, including (1) a slowdown in the economy, (2) increased foreign competition, as the strong U.S. dollar has increased the attractiveness of imported consumer goods, and (3) the increasing substitution of nonferrous components by manufacturers of consumer goods. Steel revenues increased in 1984 mainly as a result of the general economic resurgence experienced after the 1981-1982 economic recession.

Cost of products sold, as a percentage of sales, amounted to 80.0%, 81.4% and 80.8% for 1985, 1984 and 1983, respectively. The improvement in such cost in 1985 resulted mainly from the availability of more favorable quantity order prices on materials purchased than were available in 1984.

The provision for income taxes in the steel service segment, although it fluctuated in amount, represented 47.0%, 48.8% and 47.8% of pre-tax income for 1985, 1984 and 1983, respectively, not significantly different from the combined federal and state rates on ordinary income.

Steel service net income was held to a decline of only 1% for 1985 on the 7% decrease in sales revenues. The steel service business operates on a low gross margin. Thus, the slight improvement in cost of products sold was the primary factor responsible. The improvement in steel service net income in 1984 resulted principally from the increase in sales revenues.

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

In 1985, Touche Ross & Co. was selected as the independent public accountants for Wesco and its subsidiaries, in place of Peat, Marwick, Mitchell & Co. There were no disagreements between Wesco Financial Corporation ("Wesco") and its independent public accountants during any recent year with respect to any matters of accounting principles or practices or financial statement disclosures not ultimately adopted by Wesco.

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 27, 1986, 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 27, 1986, 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 27, 1986, 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 27, 1986, 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. File No. 1-4720).

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, 1985.

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 Chairman of the Board and President (principal executive officer)	March 27, 1986
By: Jeffrey L. Jacobson Vice President and Chief Financial Officer (principal financial officer)	March 27, 1986
By: Jeanne Leach Treasurer (principal accounting officer)	March 27, 1986

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 Director	March 27, 1986
H. R. Dettmann Director	March 27, 1986
David K. Robinson Director	March 27, 1986
James N. Gamble Director	March 27, 1986

REPORTS OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Shareholders of
Wesco Financial Corporation

We have examined the consolidated balance sheet of Wesco Financial Corporation and subsidiaries as of December 31, 1985, and the related statements of income and retained earnings, and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Wesco Financial Corporation and subsidiaries as of December 31, 1985, and the results of their operations and the changes in their financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Our examination also comprehended the schedules listed in the index at Item 8. In our opinion, such schedules, when considered in relation to the basic financial statements, present fairly, in all material respects, the information presented therein.

Touche Ross & Co.
Touche Ross & Co.

Los Angeles, California
February 13, 1986

To the Board of Directors and Shareholders of
Wesco Financial Corporation

We have examined the consolidated balance sheet of Wesco Financial Corporation and subsidiaries as of December 31, 1984, and the related statements of income and retained earnings and changes in financial position for each of the years in the two year period ended December 31, 1984. 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 financial statement schedules as of and for each of the years in the two year period ended December 31, 1984, 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 the results of their operations and the changes in their financial position for each of the years in the two year period ended December 31, 1984, in conformity with generally accepted accounting principles applied on a consistent basis. Also, in our opinion, the related financial statement schedules as of and for each of the years in the two year period ended December 31, 1984, 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.
Peat, Marwick, Mitchell & Co.

Los Angeles, California
January 31, 1985

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

ASSETS	December 31, 1985	December 31, 1984
Financial:		
Cash	$ 2,810	$ 1,951
Investments (Note 3):		
Short-term investments	325,299	161,397
State and municipal bonds	26,398	29,987
Common and preferred stocks	62,187	96,192
Investment in Bowery Savings Bank	9,020	—
Total investments	422,904	287,576
Loans receivable (Note 4)	83,472	95,172
Accounts receivable	13,921	2,681
Deferred insurance policy acquisition costs (Note 2)	8,254	—
Real estate held for sale	2,026	2,011
Investments required by law:		
Investment in stock of Federal Home Loan Bank, at cost	952	1,137
Prepayments to FSLIC secondary reserve	3,385	3,146
Premises and equipment, net (Note 5)	3,435	3,216
Other assets	2,190	1,932
	543,349	398,822
Steel service:		
Cash	13	13
Accounts receivable	5,433	5,318
Inventories (Note 6)	8,213	7,690
Property, plant and equipment, net (Note 5)	4,864	5,080
Other assets	85	80
	18,608	18,181
	$561,957	$417,003

LIABILITIES AND SHAREHOLDERS' EQUITY	1985	1984
Financial:		
Savings accounts (Note 7)	$269,047	$227,087
Accounts payable and accrued expenses	2,085	5,047
Unearned insurance premiums (Note 2)	26,326	—
Losses and loss adjustment expenses of insurance business (Note 2)	16,111	—
Income taxes payable (Note 8)	20,918	5,803
Notes payable (Note 9)	30,023	30,182
	364,510	268,119
Steel service:		
Accounts payable and accrued expenses	2,934	2,259
Income taxes payable (Note 8)	2,212	1,286
Notes payable (Note 9)	1,500	1,700
	6,646	5,245
Total liabilities	371,156	273,364
Commitments and contingent liabilities (Notes 11 and 12)		
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
Unrealized appreciation of marketable equity securities of insurance business (Note 3)	35	—
Retained earnings—partially restricted (Note 13)	160,327	113,200
Total shareholders' equity	190,801	143,639
	$561,957	$417,003

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,		
	1985	1984	1983
Financial:			
Revenues—			
Interest on loans	$ 6,794	$ 7,711	$ 8,567
Interest on short-term investments and on state and municipal bonds	24,651	17,170	9,294
Dividends on common and preferred stocks	6,944	7,765	9,025
Insurance premiums earned (Note 2)	20,412	—	—
Fluctuation in market value of GNMA futures contract (Note 4)	2,803	938	—
Gain on sales of marketable securities (Note 10)	62,895	19,360	3,025
Rental income of $2,219, $2,078 and $1,986, less expense of $1,123, $1,032 and $1,051	1,096	1,046	935
Other	937	906	852
	126,532	54,896	31,698
Expenses—			
Interest on savings accounts	25,191	20,940	16,870
Insurance losses and loss adjustment expenses (Note 2)	16,606	—	—
Amortization of deferred insurance policy acquisition costs (Note 2)	6,402	—	—
Interest on notes payable	3,035	3,103	4,673
General and administrative	4,031	3,347	3,452
	55,265	27,390	24,995
Income before income taxes	71,267	27,506	6,703
Income tax (provision) benefit (Note 8)	(21,736)	(5,884)	2,228
Net income—financial	49,531	21,622	8,931
Steel service:			
Revenues—			
Sales	51,124	55,098	46,074
Other	181	207	191
	51,305	55,305	46,265
Costs and expenses—			
Cost of products sold	40,914	44,830	37,220
Selling, general and administrative expenses	6,600	6,501	5,936
	47,514	51,331	43,156
Income before income taxes	3,791	3,974	3,109
Income tax provision (Note 8)	(1,781)	(1,940)	(1,487)
Net income—steel service	2,010	2,034	1,622
Net income—consolidated	51,541	23,656	10,553
Retained earnings—beginning of year	113,200	93,673	86,964
Cash dividends declared and paid	(4,414)	(4,129)	(3,844)
Retained earnings—end of year	$160,327	$113,200	$ 93,673
Amounts per share based on 7,119,807 shares:			
Net income—consolidated	$7.24	$3.32	$1.48
Cash dividends	$ .62	$ .58	$ .54

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,		
	1985	1984	1983
Financial:			
Sources (uses) of cash, including short-term investments, from operations—			
Net income	$ 49,531	$ 21,622	$ 8,931
Add (deduct):			
Depreciation and amortization, including amortization of bond premiums of $300, $421 and $421	554	721	765
Interest expense credited to savings accounts	20,845	18,061	15,537
Increase in insurance premiums receivable	(10,712)	—	—
Increase in unearned insurance premiums	26,326	—	—
Increase in deferred insurance policy acquisition costs	(8,254)	—	—
Increase in unpaid losses and loss adjustment expenses of insurance business	16,111	—	—
(Increase) decrease in current income taxes receivable	—	2,596	(91)
Increase (decrease) in income taxes payable	15,115	1,012	(368)
Other, net	145	(880)	(317)
Cash provided from financial operations	109,661	43,132	24,357
Other sources (uses) of cash—			
Principal collections on real estate loans	11,772	11,396	15,097
Increase in savings accounts, net	21,115	20,831	20,169
(Increase) decrease in state and municipal bonds and common and preferred stocks	37,294	16,248	(23,024)
Investment in Bowery Savings Bank	(9,020)	—	—
Increase (decrease) in accounts payable from purchases of common stocks	(3,435)	4,012	—
Repayment of notes payable	(159)	(1,385)	(21,056)
Payment of cash dividends	(4,414)	(4,129)	(3,844)
Other, net	(1,037)	2,471	(667)
	161,777	92,576	11,032
Steel service:			
Sources (uses) of cash from operations—			
Net income	2,010	2,034	1,622
Add (deduct):			
Depreciation and amortization	673	650	633
Decrease (increase) in receivables	(115)	40	(1,661)
Increase in inventories	(523)	(797)	(1,524)
Increase in accounts payable and accrued expenses	675	21	842
Increase in income taxes payable	926	194	769
Other, net	(5)	41	28
Cash provided from steel service operations	3,641	2,183	709
Other uses of cash—			
Additions to property, plant and equipment	(457)	(453)	(148)
Repayment of notes payable	(200)	(220)	(218)
	2,984	1,510	343
Consolidated increase in cash, including short-term investments	$164,761	$ 94,086	$ 11,375

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"), Wesco-Financial Insurance Company ("Wes-FIC"—see Note 2), 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 (see Note 2).

Note 2. Wesco-Financial Insurance Company

In August 1985 Wesco formed a wholly owned subsidiary, Wesco-Financial Insurance Company ("Wes-FIC"), to engage in the property and casualty insurance and reinsurance business, in a co-venture with its ultimate parent company, Berkshire Hathaway Inc. Wesco contributed $45 million in cash and cash-equivalents to the capital of Wes-FIC in September 1985.

Wes-FIC, as its initial transaction, entered into a reinsurance agreement with National Indemnity Company ("NICO"), an insurance subsidiary of Berkshire, which acts as an intermediary-without-profit. Under terms of the agreement, Wes-FIC participates proportionately (2%) in all premiums, losses and expenses of in-force business of Fireman's Fund Insurance Companies ("FFC") for a term of four years from September 1, 1985. No other insurance transactions have been entered into by Wes-FIC.

Wes-FIC's premiums written in 1985 represent 2% of FFC's unearned premiums at September 1, 1985, plus 2% of FFC's premiums written in the months of September through December. Likewise, Wes-FIC's 1985 costs, other than its nominal organizational expense, represent 2% of FFC's costs relating to the risks with respect to which premiums were earned during the last four months of 1985. For insurance premiums written, commissions of $14,656 were paid through NICO to FFC, representing a pro rata share of FFC's own acquisition costs. Of such amount, $8,254 is recorded in the accompanying balance sheet at December 31, 1985 as deferred insurance policy acquisition costs. These deferred costs are deemed recoverable from premiums written during the year but unearned at 1985 yearend. In determining recoverability of such costs, Wes-FIC has taken into account investment income conservatively anticipated to be earned on funds held under the contract.

Following are summarized financial statements for Wes-FIC for the four months of its operations in 1985:

Wesco-Financial Insurance Company
Condensed Statement of Operations

	Four Months Ended December 31, 1985
Insurance premiums written	$46,738
Less unearned premiums at December 31, 1985	26,326
Insurance premiums earned	20,412
Interest and dividend income	2,219
	22,631
Losses and loss adjustment expenses	16,606
Amortization of deferred acquisition costs	6,402
Policyholder dividends	338
	23,346
Loss before income tax benefit	(715)
Income tax benefit	356
Net loss	$ (359)

Wesco-Financial Insurance Company
Condensed Balance Sheet

ASSETS	December 31, 1985
Cash and short-term investments	$61,007
State and municipal bonds	3,784
Marketable equity securities, at market value	6,592
Premiums receivable	10,712
Deferred insurance policy acquisition costs	8,254
Other assets	1,630
	$91,979
LIABILITIES AND SHAREHOLDER'S EQUITY	
Losses and loss adjustment expenses	$16,111
Unearned premiums	26,326
Deferred income taxes	3,659
Other liabilities	1,207
Total liabilities	47,303
Shareholder's equity:	
Capital stock	1,000
Paid-in capital	44,000
Unrealized appreciation of marketable equity securities, net	35
Deficit, representing net loss for the four months ended December 31, 1985	(359)
Total shareholder's equity	44,676
	$91,979

Note 3. Investments

Marketable equity securities are carried on the consolidated balance sheet principally at the lower of aggregate cost or market, except for those held in the insurance business (see Note 2), which are carried at market value. Any unrealized gain or loss resulting from such carrying values is added to or deducted from shareholders' equity on the consolidated balance sheet, net of deemed applicable income taxes, without effect on net income.

Short-term investments (mainly securities issued by the U.S. Government and obligations of the Federal Home Loan Bank or other U.S. Government Agencies) and state and municipal bonds, are stated at cost, adjusted for amortization of premium and accretion of discount.

Following is a summary of marketable securities at yearend:

	1985			1984		
	Cost	Market	Carrying Value	Cost	Market	Carrying Value
Short-term investments	$325,299	$326,549	$325,299	$161,397	$164,527	$161,397
State and municipal bonds	$ 26,398	$ 29,747	$ 26,398	$ 29,987	$ 32,543	$ 29,987
Marketable equity securities—						
Common stocks	$ 26,486	$ 26,763	$ 26,535	$ 65,862	$ 80,177	$ 65,862
Preferred stocks	34,146	38,788	34,146	27,724	26,349	27,724
	60,632	65,551	60,681	93,586	106,526	93,586
Other preferred stocks	1,506	1,245	1,506	2,606	2,334	2,606
	$ 62,138	$ 66,796	$ 62,187	$ 96,192	$108,860	$ 96,192

At December 31, 1985, the consolidated portfolio of marketable equity securities contained aggregate unrealized gains of $6,171 and aggregate unrealized losses of $1,252.

In addition to the investments in marketable securities summarized above, Wesco has an equity investment, at cost of $9,020, in approximately 9% of a newly organized, New York-chartered savings bank, which recently took over the name, $5 billion in assets and liabilities of the insolvent Bowery Savings Bank in the city of New York. The takeover was assisted by the Federal Deposit Insurance Corp. ("FDIC"), the federal agency, akin to FSLIC, which insures deposits in banks. Although terms of such FDIC assistance include future income-assistance payments, management of Wesco considers this investment to be essentially of the venture-capital type, with prospects for ultimate gain justifying the high risk of loss.

Dollar amounts in thousands except for amounts per share

Note 4. Loans Receivable

Following is a summary of loans receivable by type of collateral at yearend:

	1985	1984
Residential property of one to four units	$ 70,449	$ 80,329
Residential property of more than four units	9,396	11,147
Commercial property and vacant land	3,107	3,275
Savings accounts	565	493
	83,517	95,244
Less unearned loan fees and unrealized profit on sales of real estate	(45)	(72)
	$ 83,472	$ 95,172
Average interest rate	7.60%	7.63%

Interest income on loans is recognized under the accrual method of accounting. Such accrued interest amounted to $310 and $368 at 1985 and 1984 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. Generally accepted accounting principles require that earnings reflect fluctuations in market value of futures contracts. The unrealized gains for 1985 and 1984 of $2,803 and $938 before income taxes, are reflected on the accompanying consolidated statement of income in the category fluctuation in market value of GNMA futures contract. No additional gain or loss was realized on sale of the contract in 1985.

Note 5. Property, Plant, Premises and Equipment

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

	1985	1984
Financial:		
Land	$1,386	$1,386
Office, store and garage buildings and leasehold improvements	6,624	6,217
Furniture, fixtures and equipment	898	832
	8,908	8,435
Less accumulated depreciation and amortization	5,473	5,219
	$3,435	$3,216
Steel service:		
Land	$ 640	$ 640
Buildings and improvements	2,915	2,907
Machinery and equipment	5,137	4,729
	8,692	8,276
Less accumulated depreciation and amortization	3,828	3,196
	$4,864	$5,080

The financial and a portion of the steel service land and buildings collateralize certain debt. See Note 9.

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

Note 6. 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 $4,371 and $4,900 at yearend in 1985 and 1984.

The decline in difference between LIFO and FIFO valuation during 1985 was caused by a decrease in unit purchasing costs during the year; total inventory quantities increased slightly. This decline in costs resulted in a decrease in cost of products sold and, thus, an increase in net income of approximately $264 or $.04 per share.

Dollar amounts in thousands except for amounts per share 31

Note 7. Savings Accounts

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

Type of Account	Interest Rate [a]	1985	1984
Interest-bearing checking accounts[b]	5.25%	$ 1,856	$ 1,586
Passbook accounts[b]	5.50	13,286	14,771
Money market rate accounts[b]	6.96	65,988	56,207
Certificate accounts:			
7–31 days	7.70	456	517
32 days–6 months	7.56	27,305	33,361
7 months–1 year	8.70	14,478	13,906
13 months–2 years	10.19	47,363	23,621
25 months–4 years	11.34	59,199	54,019
Over 4 years	9.43	1,672	1,074
IRA/Keogh accounts, 18 months[c]	11.34	25,592	12,677
Jumbo certificates of deposit	9.06	8,418	10,952
Other accounts	7.62	3,434	4,396
		$269,047	$227,087

[a] Weighted average interest rate at 1985 yearend.
[b] No stated maturity.
[c] Other IRA/Keogh accounts included in the various certificate accounts amounted to $879 and $2,967 at 1985 and 1984 yearends.

The weighted average interest rates on all accounts at 1985 and 1984 yearends were 9.07% and 10.37%. 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 1985, certificate accounts mature as follows: 1986, $148,549; 1987, $26,636; 1988, $8,803; 1989, $3,788; 1990, $89; thereafter, $52.

Note 8. Taxes on Income

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

	1985	1984	1983
Applicable to:			
Financial	$21,736	$ 5,884	$ (2,228)
Steel service	1,781	1,940	1,487
	$23,517	$ 7,824	$ (741)

These taxes are payable or recoverable as follows:

	1985	1984	1983
Payable (recoverable) currently—			
Federal	$15,097	$ 5,179	$ (977)
State	6,133	2,634	504
	21,230	7,813	(473)
Payable (recoverable) in the future—			
Federal	2,273	(9)	(279)
State	14	20	11
	2,287	11	(268)
	$23,517	$ 7,824	$ (741)

Dollar amounts in thousands except for amounts per share

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, deferred income taxes, are included in income taxes payable 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:

	1985	1984	1983
Insurance policy acquisition costs deducted on cash basis for tax purposes vs. accrual basis on the books	$ 3,797	$ —	$ —
Loan fees recognized under a different method for tax purposes	(339)	(316)	(435)
State income taxes deducted on cash basis for tax purposes vs. accrual basis on the books	(1,234)	(959)	(724)
Mutual Savings' income recognized on cash basis for tax purposes vs. accrual basis on the books	(411)	230	(18)
Other timing differences	474	1,056	909
Total taxes payable (recoverable) in the future	$ 2,287	$ 11	$ (268)

The income tax provision of $23,517 for 1985 amounted to 31.3% of pre-tax income of $75,058, the provision of $7,824 for 1984 amounted to 24.9% of pre-tax income of $31,480, and the benefit of $741 for 1983 represented 7.6% of pre-tax income of $9,812. Following is a summary of the differences between the federal statutory rate and these effective income tax rates:

	1985	1984	1983
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	(5.2)	(11.1)	(36.0)
100% exclusion from taxable income of interest on state and municipal bonds	(1.8)	(4.7)	(15.1)
Use of lower rate on capital gains	(13.2)	(9.9)	(5.5)
State income taxes, net of federal income tax benefit	4.4	4.6	2.4
Other differences, net	1.1	—	.6
Effective income tax (benefit) rate	31.3%	24.9%	(7.6)%

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. 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 1980 have been examined by and settled with the Internal Revenue Service.

Dollar amounts in thousands except for amounts per share

Note 9. Notes Payable

Following is a list of notes payable at yearend:

	1985	1984
Wesco—		
Notes due June 1991, currently redeemable at 104% of face value declining to 100% by 1989, bearing interest at 10⅛%, payable in semiannual installments	$25,000	$25,000
Notes payable, collateralized by land, buildings and assignment of leases, due in monthly installments through February 2007 of $45 including interest at 9¼%	5,023	5,182
Total financial	$30,023	$30,182
Precision Steel—		
Industrial revenue bonds, guaranteed by Wesco, due in quarterly installments through December 1994 of $42 plus interest at 6½%	$ 1,500	$ 1,665
Notes payable, collateralized by land and buildings, due in monthly installments through July 1985 of $5 including interest at 5½%	—	35
Total steel service	$ 1,500	$ 1,700

Notes payable at yearend in 1985 mature as follows:

	Consolidated	
Year	Financial	Steel Service
1986	$ 66	$ 167
1987	72	167
1988	78	167
1989	87	167
1990	95	167
Thereafter	29,625	665
	$30,023	$ 1,500

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 10. Gain on Sales of Marketable Securities

Following is a summary of pre-tax gain on sales of marketable securities for each of the past three years:

	1985	1984	1983
Special share redemption proceeds received from General Foods Corporation, less cost of shares redeemed	$ 639	$ 1,206	$ —
Gain on sale of General Foods stock to Philip Morris Company under tender offer	50,539	—	—
Pre-tax gain realized on other sales of marketable securities	11,717	18,154	3,025
	$62,895	$19,360	$ 3,025

Wesco and certain of its subsidiaries (the "Wesco Group") sold their investment in General Foods Corporation common stock late in 1985 to Philip Morris Company in connection with the latter's tender offer at a large premium over the previously-prevailing market price of General Foods' stock. Prior thereto, the Wesco Group had received redemption proceeds from General Foods in connection with its publicly announced share repurchase program. Such dividend-equivalent proceeds, which amounted to $1,287 and $3,177 in 1985 and 1984, and which are taxed at the Federal rate of 6.9% applicable to dividend income, are reflected as securities gains in the accompanying consolidated statement of income, after reduction for cost of the shares redeemed, as required by generally accepted accounting principles.

Dollar amounts in thousands except for amounts per share

Note 11. Lease Commitments and Rental Expense

At yearend in 1985, Wesco and its subsidiaries have future minimum rental commitments as follows: 1986, $376; 1987, $352; 1988, $192; 1989, $41; 1990, $27; thereafter, none. Rental expense amounted to $469, $456 and $421 in 1985, 1984 and 1983.

Note 12. 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 1985, 1984 and 1983 amounted to $47, $60 and $52.

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 1985, 1984 and 1983 were $167, $162 and $158.

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, 1985, for the financial segment and June 1, 1985, for the steel service segment (dates of the most recent actuarial valuations). The rates of return assumed in determining present values ranged from 6% to 8%.

	Financial	Steel Service
Actuarial present value of accumulated plan benefits:		
Vested	$ 509	$1,494
Nonvested	14	63
	$ 523	$1,557
Net assets available for benefits	$1,311	$2,054

Note 13. Retained Earnings

Retained earnings of Wesco include $47,314 of undistributed retained earnings of Mutual Savings, which were taken as special bad debt deductions for income tax purposes through 1968, after which such deductions were no longer available to Mutual Savings due to its having reached certain limitations. These deductions are not related to amounts of losses actually anticipated and have not been charged against book income. If, in the future, any portion of such retained earnings is used for any purpose other than to absorb loan losses, including payment of dividends to Wesco 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 $6,300, plus future earnings on a tax-return basis. (Dividends of $14,000 were paid in 1985; none were paid in 1984 or 1983.)

Dollar amounts in thousands except for amounts per share 35

Note 14. Quarterly Financial Information

Unaudited quarterly financial information for 1985 and 1984 follows:

	Quarter Ended			
	December 31, 1985	September 30, 1985	June 30, 1985	March 31, 1985
Financial revenues	$ 77,568	$ 21,660	$ 17,345	$ 9,959
Interest expense—savings accounts	(6,298)	(6,497)	(6,334)	(6,062)
Steel service revenues	12,505	12,630	12,605	13,565
Cost of steel products sold	(9,455)	(10,284)	(10,095)	(11,080)
Net income	35,936	6,469	6,301	2,835
Per share	5.05	.91	.88	.40
Securities gains, less securities losses, net of income tax effect, included in net income above	34,284	4,182	2,964	93
Per share	4.81	.59	.42	.01
	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	—

Dollar amounts in thousands except for amounts per share

WESCO FINANCIAL CORPORATION
SCHEDULE I—MARKETABLE SECURITIES

DECEMBER 31, 1985
(Dollar amounts in thousands)

Name of Issuer and Title of Each Issue	Number of Shares of Stock or Principal Amount of Notes	Cost	Market Value	Balance Sheet Carrying Value
Securities held by the consolidated group were as follows:				
Short-term investments—				
Securities of U.S. Government and obligations of the Federal Home Loan Bank and other U.S. Government Agencies	$320,305	$319,538	$320,559	$319,538
Other	5,738	5,761	5,990	5,761
Total short-term investments		$325,299	$326,549	$325,299
State and municipal bonds	$ 29,930	$ 26,398	$ 29,747	$ 26,398
Common stocks—				
Beatrice Corporation	581,800	$ 26,486	$ 26,763	$ 26,535
Preferred stocks—				
Various issues, primarily public utilities	950,865	$ 35,652	$ 40,033	$ 35,652

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

Name of Issuer and Title of Each Issue	Number of Shares of Stock or Principal Amount of Notes	Cost	Market Value	Balance Sheet Carrying Value
Held by Wesco Financial Corporation (registrant)—				
U.S. Government securities	$ 58,345	$ 58,061	$ 58,123	$ 58,061
Other short-term investments	1,130	1,120	1,190	1,120
		$ 59,181	$ 59,313	$ 59,181
Held by Precision Steel Warehouse, Inc. (wholly owned subsidiary of Wesco Financial Corporation)—				
U.S. Government securities	$ 47,082	$ 47,001	$ 47,587	$ 47,001
Other short-term investments	2,952	2,999	3,057	2,999
		$ 50,000	$ 50,644	$ 50,000
Held by Wesco-Financial Insurance Company (wholly owned subsidiary of Wesco Financial Corporation)—				
U.S. Government securities	$ 61,272	$ 60,982	$ 60,982	$ 60,982
Beatrice Corp. common stock	143,300 shares	6,543	6,592	6,592
		$ 67,525	$ 67,574	$ 67,574
Held by Wes-Fin Service Corp. (wholly owned subsidiary of Mutual Savings and Loan Association)—				
U.S. Government securities	$ 9,305	$ 9,252	$ 9,359	$ 9,252
Beatrice Corp. common stock	438,500 shares	19,943	20,171	19,943
		$ 29,195	$ 29,530	$ 29,195

Individual issues with a cost or market value equal to or exceeding 2% of total assets at December 31, 1985, are stated separately.

Marketable equity securities held by the insurance subsidiary are carried at market value on the consolidated balance sheet; those held by the registrant and its other subsidiaries are carried at the lower of aggregate of cost or market.

WESCO FINANCIAL CORPORATION
SCHEDULE III—CONDENSED FINANCIAL INFORMATION OF REGISTRANT
BALANCE SHEET
(Dollar amounts in thousands)

	December 31, 1985	December 31, 1984
ASSETS		
Cash (including savings accounts at Mutual Savings of $224 and $403)	$ 284	$ 434
Short-term investments	59,181	54,700
Common stocks, at cost (market $21,973 in 1984)	—	12,613
Investment in Bowery Savings Bank	9,020	—
Advance to subsidiary	4,200	4,200
Investment in subsidiaries, at equity:		
Mutual Savings	57,579	62,249
Precision Steel	53,322	36,696
Wes-FIC	44,676	—
Others	120	74
	155,697	99,019
Premises and equipment, net	3,194	3,069
Other assets	567	748
	$232,143	$174,783
LIABILITIES AND SHAREHOLDERS' EQUITY		
Notes payable	$ 30,023	$ 30,182
Accounts payable and accrued expenses	500	506
Income taxes payable	10,819	456
Total liabilities	41,342	31,144
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	160,327	113,200
Equity in unrealized appreciation of marketable equity securities of insurance subsidiary	35	—
Total shareholders' equity	190,801	143,639
	$232,143	$174,783

See notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION
SUPPLEMENTARY INSURANCE INFORMATION
(Dollar amounts in thousands)
SCHEDULE V

Segment	Deferred Policy Acquisition Costs	Future Claim and Loss Expenses	Unearned Premiums	Earned Premiums	Net Investment Income	Loss and Loss Adjustment Expenses Incurred	Amortized Deferred Policy Acquisition Costs	Other Underwriting Expenses	Written Premiums
1985									
Property and casualty reinsurance ...	$8,254	$16,111	$26,326	$20,412	$2,219	$16,606	$6,402	—	$46,738

WESCO FINANCIAL CORPORATION
SCHEDULE III—CONDENSED FINANCIAL INFORMATION OF REGISTRANT
STATEMENT OF INCOME AND RETAINED EARNINGS
(Dollar amounts in thousands)

	Year Ended December 31,		
	1985	1984	1983
Revenues—			
Dividends on common stocks	$ 874	$ 2,208	$ 3,189
Interest on short-term investments	4,908	3,138	—
Interest on savings accounts at Mutual Savings	66	1,048	1,510
Rental of office, store and garage premises, net	1,771	1,694	1,558
Dividends from subsidiaries	14,075	—	—
Gain on sales of marketable securities	35,995	10,635	218
Other	38	30	62
	57,727	18,753	6,537
Expenses—			
Interest on notes payable	3,034	3,086	3,017
General and administrative	605	576	577
	3,639	3,662	3,594
Income before items shown below	54,088	15,091	2,943
Income tax provision	(14,086)	(4,907)	(242)
Equity in undistributed earnings of subsidiaries	11,539	13,472	7,852
Net income	51,541	23,656	10,553
Retained earnings—beginning of year	113,200	93,673	86,964
Cash dividends	(4,414)	(4,129)	(3,844)
Retained earnings—end of year	$160,327	$113,200	$ 93,673

See notes to consolidated financial statements.

WESCO FINANCIAL CORPORATION
SCHEDULE X—SUPPLEMENTARY INCOME STATEMENT INFORMATION
(Dollar amounts in thousands)

	Consolidated		
	Financial	Steel Service	Registrant
1985:			
Maintenance and repairs	$425	$290	$333
Property taxes	98	195	82
Advertising	97	267	—
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	—

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

	December 31, 1985	December 31, 1984
ASSETS		
Cash and short-term investments	$157,766	$ 92,185
State and municipal bonds, at cost (market $25,958 and $32,543)	22,608	29,987
Marketable equity securities, at lower of aggregate cost or market:		
Common stocks—		
Owned by Mutual Savings (cost $14,802 in 1984)	—	15,201
Owned by service subsidiary (market $20,171 in 1985; cost $22,245 in 1984)	19,943	22,523
Preferred stocks owned by Mutual Savings (market $38,788 in 1985; cost $27,724 in 1984)	34,146	26,349
Other marketable securities, at cost:		
Preferred stocks (market $1[illegible]5 and $2,334)	1,506	2,606
Loans receivable, principally real estate, yielding 7.60% and 7.63%	83,425	95,120
Income taxes receivable	1,450	761
Real estate held for sale	2,026	2,011
Investment in stock of Federal Home Loan Bank and prepayments to FSLIC secondary reserve	4,337	4,283
Other assets	4,390	4,016
	$331,597	$295,042
LIABILITIES AND SHAREHOLDER'S EQUITY		
Savings accounts	$269,313	$227,585
Accounts payable and accrued expenses	376	474
Deferred income taxes	4,329	5,432
	274,018	233,491
Shareholder's equity:		
Guarantee stock and additional paid-in capital	100	100
Retained earnings—substantially restricted	57,479	62,149
Net unrealized loss on marketable equity securities	—	(698)
Total shareholder's equity	57,579	61,551
	$331,597	$295,042
Cash dividends declared and paid	$ 14,000	—

See notes to consolidated financial statements of Wesco Financial Corporation.

Main entrance to Mutual Savings' head office.

MUTUAL SAVINGS AND LOAN ASSOCIATION

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