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DIVERSIFIED RETAILING CO INC

10-K

1974

OTHER

CARD 1

Diversified Retailing Company, Inc. [Md.] Co: D674000000
1300 Mercentile Bank & Trust Building
2 Hopkins Plaza
Baltimore, Md. 21201
SEC File No: 2-27473 Exch: Other
IRS No: 52-0846159 CUSIP: 2553279
Fiscal Year Ends: 1/31 SIC No: 531

10-K For: 2/3/73 Rec: 5/4/73
Auditor: Ernst & Ernst
Revenues: $38,918,071 Earnings: $2,918,042/$2.92
Assets: $27,855,906 Net Worth: $17,920,000
Extr. Items: $193,021 Shareholders: 275

Description of Business: Holds Associated Retail Stores, Inc. which operates 68 stores selling women's and children's apparel in 9 states in leased or owned premises. Subsidiary engages in accepting portions of reinsurance contracts.

- Holding companies
- Apparel retailing; Womens apparel retailing; Childrens apparel retailing

Auditor's Report:

- Qualified opinions for uncertainties; Asset realization; Equity method of carrying investment; Unconsolidated subsidiaries; Civil court proceedings
- Qualified opinions for consistency; Accounting principle changes; Equity method of carrying investment; *Blue Chip Stamps; *Berkshire Hathaway Inc.

Financial Statements and Notes:

- Exchange of securities; Extraordinary gains
- Negative goodwill; Goodwill amortized under 40 years
- Unconsolidated insurance subs; *Columbia Insurance Co.
- Asset acquisition; Investments; Dealings with related persons

Exhibits: None indexed.

8-K For: 5/31/73 Rec: 6/11/73
Withdrew suit challenging condemnation of property held by its subsidiary, Associated Retail Stores, Inc.; matter now settled. $1,482,904 received from Philadelphia Redevelopment Authority as condemnation settlement.

- Out of court litigation settlement; Condemnation; *Philadelphia Redevelopment Authority
- Extraordinary real estate sale gains; Condemnation

Exhibits: None indexed

10-Q For: 5/5/73 Rec: 6/19/73

8-K For: 7/31/73 Rec: 8/2/73
Application filed with Federal Savings and Loan Insurance Corp. seeking approval of the indirect acquisition of Mutual Savings and Loan Association, which is required when an insured institution is acquired by other than a savings and loan holding company.

- Investment increase; *Wesco Financing Corp.; Regulatory approval pending; Indirect investments; Savings and loan holding companies

Exhibits: None

10-Q For: 8/4/73 Rec: 2/18/73

10-Q For: 11/3/73 Rec: 12/18/73

LEASCO

D674000

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
February 2, 1974

Commission file number:
2-27473

DIVERSIFIED RETAILING COMPANY, INC.

State of Incorporation: Maryland

I.R.S. Employer Identification No.
52-0846159

Address of principal executive offices:
1300 Mercantile Bank & Trust Building
2 Hopkins Plaza
Baltimore, Maryland 21201

Registrant's telephone number, including area code: (301)547-0500

Securities Registered Pursuant to Section 12(b) of the Act:

None.

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 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes __X__. No _____.

PART I

ITEM 1. BUSINESS.

A. General

Diversified Retailing Company, Inc. (hereinafter referred to as "the Company"), a Maryland corporation, is a holding company which renders financial and operating advice to its wholly-owned subsidiary, Associated Retail Stores, Inc. (hereinafter referred to as "Associated") and to Associated's subsidiaries. The Company also owns certain marketable securities. The Company has no direct salaried employees and (with certain nominal exceptions noted under ITEM 12. DIRECTORS OF REGISTRANT and/or under ITEM 13. REMUNERATION OF DIRECTORS AND OFFICERS) does not compensate its Directors and Officers for their services. The Company's President, Robert M. Goldman, acts upon material corporate matters only with the approval of the Board of Directors of the Company.

B. Associated Retail Stores, Inc.

Associated, an Illinois corporation, is the Company's wholly-owned subsidiary. Associated operates a chain of stores which sell at retail popularly priced women's and, in a number of stores, children's apparel. The stores are located in downtown, neighborhood and shopping center retail areas of principal cities in ten (10) states, in leased or owned premises (see ITEM 3. PROPERTIES), and operate under various trade names.

Associated seeks to afford its customers a wide variety of available merchandise while reducing its overhead costs to as low a level as is possible. Because of the number of stores operated by Associated, it is able to practice certain economies of scale. All of Associated's stores are served by a central buying and warehousing organization located in New York City, from which the stores' apparel

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NOTE: Unless the text otherwise indicates, all statements made in PART I describe circumstances existing as of February 2, 1974.

lines are administered. A staff of merchandise managers and buyers maintains daily personal contact with the apparel markets located in New York City and elsewhere. Nearly all receiving and purchasing activities are conducted in the central warehouse, from which shipments are made daily to the various stores. Associated utilizes detailed inventory control and analysis procedures, primarily through the use of a leased computer system, to identify popular and fast-selling items for rapid replacement, and to identify those items requiring an immediate reduction in price so that they may be sold quickly. In addition, Associated utilizes interchangeable store fixtures to facilitate the opening and closing of its stores. Associated's policy of making sales only for cash or on credit under approved bank charge account plans has allowed it further to avoid unnecessary overhead costs.

In recent years sales volume on a store-by-store basis has been declining. This trend has caused a narrowing of Associated's operating profit margins.

Associated regularly employs approximately fifteen hundred (1,500) full and part-time employees, and seasonally employs an additional two hundred (200) employees. All of its sales personnel are paid at an hourly rate, and none are paid sales commissions. Approximately eighty percent (80%) of Associated's employees are covered by union contracts which expire at various times. There were no significant changes in employee relations during the fiscal year ended February 2, 1974, and Associated's management considers its relations with its employees to be satisfactory.

The business of most of the stores, particularly those in the larger cities, involves intense competition with other stores selling similar merchandise, including discount and department stores, specialty shops and stores operated by national chains.

As discussed under ITEM 3. PROPERTIES and ITEM 5. PENDING LEGAL PROCEEDINGS, two premises upon which Associated operates stores in Philadelphia, Pennsylvania, have been the subject of condemnation proceedings. During the fiscal year ended February 2, 1974, the combined gross sales of the two stores were approximately $2,530,838.00, which amount represents approximately 6.8% of aggregate gross sales of all stores operated by Associated. During the pendency of, and subsequent to, those proceedings Associated has occupied each of these premises on a month-to-month lease, but one of the leases has been terminated effective April 20, 1974. Associated is continuing to seek suitable relocation premise for these stores in Philadelphia but cannot at this time state with assurance that it will be able to resume operation of either store in the Philadelphia market.

In addition to operating the chain of retail stores, Associated wholly owns three (3) subsidiaries:

(1) Fashion Outlet of Michigan, Inc.

Fashion Outlet of Michigan, Inc. (hereinafter referred to as "Fashion Outlet"), a Michigan corporation, is a wholly-owned subsidiary of Associated which operates, on leased premises, a single popularly priced women's and children's apparel store in Saginaw, Michigan. The store is operated under the name "Fashion Outlet" so as to allow Fashion Outlet to retain the right to use that name in Michigan. The store is similar in its method of operation to a majority of the stores operated directly by Associated. The store is operated by a staff employed by Fashion Outlet.

(2) Anbec, Inc.

Anbec, Inc. (hereinafter referred to as "Anbec"), an Illinois corporation, is a wholly-owned subsidiary of Associated, the sole business of which consists of the ownership of certain improved real property located in Chicago, Illinois, and the leasing of that property to Associated for the latter's operation of one of its retail stores. Anbec has no employees.

(3) Columbia Insurance Company

Columbia Insurance Company* (hereinafter referred to as

* Formerly "Reinsurance Corp. of Nebraska".

"Columbia"), a Nebraska corporation, is a wholly-owned subsidiary of Associated which engages solely in the business of accepting portions of reinsurance contracts. Columbia operates under a certificate of authority to transact the business of insurance (with the exceptions of life and title insurance) issued by the Department of Insurance of the State of Nebraska, and is currently licensed to conduct one or more insurance businesses in eleven (11) other states. At present, Columbia's business consists solely of the acceptance of portions of reinsurance contracts generated through and offered to Columbia by the reinsurance division of National Indemnity Company (hereinafter referred to as "National Indemnity"). When Columbia accepts from National Indemnity the portion of a reinsurance contract so offered to it, Columbia generally pays to National Indemnity a commission of one-half (1/2) of the standard commission applicable to such business, which standard commission normally is one percent (1%) on "pro rata" business and ten percent (10%) on certain "excess" business. In consideration of Columbia's payment to National Indemnity of such commission, National Indemnity manages the bookkeeping and other internal technical affairs of Columbia.

Substantially all of the common stock of National Indemnity is owned by Berkshire Hathaway, Inc. (hereinafter referred to as "Berkshire"), a Delaware corporation. Although as of February 2, 1974, Warren E. Buffett, a member of his immediate family, the Company and its subsidiaries owned substantial amounts of the common stock of Berkshire and although Mr. Buffett is the Chairman of the Board of Directors of the Company, of Associated, of Columbia, and of Berkshire (see <u>ITEM 4. PARENTS AND SUBSIDIARIES</u> and <u>ITEM 12. DIRECTORS OF REGISTRANT</u>), National Indemnity is not obligated to offer all or any portion of any reinsurance contract to Columbia. Accordingly, Columbia cannot be certain that it will continue to be offered business through the reinsurance division of National Indemnity, presently its only source of business. Columbia currently is completely dependent upon the continuance of its business arrangements with National Indemnity since Columbia has no independent staff for generating or evaluating business, settling losses or handling other administrative details.

The Company believes that its operations and those of Associated and its subsidiaries have at all times been conducted in accordance with the requirements imposed upon them by the federal wage-price controls.

C. Lines of business and classes of similar products or services

The Company's primary line of business (conducted through its subsidiary, Associated) is the retail sale of women's and children's apparel. Both prior to the fiscal year ended January 29, 1972, and during the fiscal years ended February 3, 1973 and February 2, 1974, that line of business was the Company's only line of business accounting for more than fifteen percent (15%) of either the Company's total sales and revenues or the Company's income (or loss) before taxes and extraordinary items. During the fiscal year ended January 29, 1972, the reinsurance business of the Company's subsidiary's unconsolidated insurance subsidiary, Columbia, represented a second such line of business.

The following table indicates the percentages of (1) total sales and revenues, and (2) income (or loss) before income taxes, equity in earnings of affiliated companies and extraordinary items, attributable to each such line of business during the last five (5) fiscal years:

	Line of business			
	the retail sale of women's and children's apparel		reinsurance	
Fiscal year ended	% of total sales and revenues	% of consolidated income (or loss) before income taxes, equity in earnings of affiliated companies and extraordinary items (a)	% of total sales and revenues	% of consolidated income (or loss) before income taxes, equity in earnings of affiliated companies and extraordinary items (a)
January 31, 1970 (c)	100%	100%	(b)	(b)
January 30, 1971	99.7%	99.5%	0.3%	0.5%
January 29, 1972	97.6%	80.5%	2.4%	19.5%
February 3, 1973	95.8%	97.3%	4.2%	2.7%
February 2, 1974	94.8%	87.3%	5.2%	12.7%

Inasmuch as each line of business involves one and only one class of similar products and/or services, the percentages enumerated for a line of business are equally correct for the respective class involved therein.

(a) The Company has no operations other than those of Associated and its subsidiaries; its loss before income taxes and extraordinary items has been excluded in computing these percentages.

(b) Prior to the fiscal year ended January 30, 1971, the Company did not engage in the business of reinsurance.

(c) The figures do not reflect the operations of Hochschild-Kohn & Co., Inc., a department store subsidiary of the Company which was sold by the Company in December, 1969.

ITEM 2. SUMMARY OF OPERATIONS.

A. Summary of consolidated operations (in thousands of dollars)
Diversified Retailing Company, Inc. and subsidiary

	Fiscal year ended February 2, 1974	February 3, 1973	January 29, 1972 (e)	January 30, 1971 (e)	January 31, 1970 (e)
Net sales	$38,399	$38,918	$38,598	$39,832	$39,113
Cost of goods sold	25,023	25,428	25,688	26,444	26,443
Interest and financing cost	720	687	673	647	565
Taxes on income	427	665	617	1,231	1,301
Earnings of continuing operations before equities of unconsolidated subsidiary and affiliated companies and extraordinary item	483	597	577	1,247	1,017
Earnings related to discontinued operations less applicable income taxes					403
Equity in earnings of unconsolidated subsidiary	913	955	621	93	
Equity in earnings of affiliated companies	1,191	1,173	429	380	13
Extraordinary gain (loss) (a), (c), (d), (f)	396	193	(111)		(1,319)
Net earnings	2,982	2,918	1,516	1,720	114
Earnings per share (b):					
Earnings of continuing operations before equities in earnings of unconsolidated subsidiary and affiliated companies and extraordinary item	$ .48	$ .60	$ .58	$ 1.25	$ 1.02
Earnings related to discontinued operations less applicable income taxes					.40
Equity in earnings of unconsolidated subsidiary	.91	.96	.62	.09	.01
Equity in earnings of affiliated companies	1.19	1.17	.43	.38	(1.32)
Extraordinary gain (loss)	.40	.19	(.11)		
Net earnings	2.98	2.92	1.52	1.72	.11
Cash dividends per share	None	None	None	None	None

DISCLOSURE® IF THE ABOVE PAGE IS LESS CLEAR THAN THIS STATEMENT, IT IS DUE TO POOR PHOTOGRAPHIC QUALITY OF THIS DOCUMENT.

(a) The extraordinary loss for fiscal 1970 resulted from the sale of a subsidiary and is shown net of $83,000 of income taxes on taxable gain.

(b) Earnings per share have been restated to reflect a 3,333 1/3-to-1 stock split which occurred in December, 1969.

(c) The extraordinary loss for fiscal 1972 resulted from additional income taxes related to the sale of the subsidiary referred to in note (a) above.

(d) The extraordinary gain for fiscal 1973 resulted from the taxable gain on an exchange of securities and is shown net of $83,000 of income taxes.

(e) Restated to reflect a change in 1973 to the equity method of accounting for investments in affiliated companies.

(f) The extraordinary gain for fiscal year 1974 resulted from condemnatio of real estate and improvements and is shown net of $213,000 of income taxes.

B. Statement of consolidated additional paid-in capital and earnings retained in the business

Diversified Retailing Company, Inc. and Subsidiary

Five years ended February 2, 1974
(in thousands of dollars)

	Additional paid-in capital	Earnings retained in the business
Balance at February 1, 1969	$6,000	5,652
Net earnings for the year ended January 31, 1970		114
Balance at January 31, 1970	6,000	5,766
Net earnings for the year ended January 30, 1971		1,720
Unrealized appreciation of marketable securities of unconsolidated insurance subsidiary of Associated Retail Stores, Inc., less provision for income taxes		384
Balance at January 30, 1971	6,000	7,870
Net earnings for the year ended January 29, 1972		1,516
Reversal of unrealized appreciation of marketable securities of unconsolidated insurance subsidiary of Associated Retail Stores, Inc., less provision for income taxes		(384)
Balance at January 29, 1972	6,000	9,002
Net earnings for the year ended February 3, 1973		2,918
Balance at February 2, 1973	6,000	11,920
Net earnings for the year ended February 2, 1974		2,982
Balance at February 2, 1974	$6,000	$14,902

NOTE: The use of parentheses ( ) indicates a deduction. The notes to the consolidated financial statements are made a part hereof.

ITEM 3. PROPERTIES.

A. General

The operating offices of the Company are located in the law offices of the firm of Frank, Bernstein, Conaway and Goldman, 1300 Mercantile Bank and Trust Building, 2 Hopkins Plaza, Baltimore, Maryland 21201, in which firm Robert M. Goldman, the President of the Company and Max E. Blumenthal, the Secretary of the Company, are partners. The Company pays no rent for the said offices and, except for certain legal and bookkeeping activities, only limited operational activities of the Company take place therein.

B. Associated Retail Stores, Inc.

The stores operated by Associated (see ITEM 1. BUSINESS) range in size of floor area from approximately two thousand (2,000) square feet to approximately sixty thousand (60,000) square feet. The total floor area of all of the stores is approximately nine hundred thousand (900,000) square feet.

Associated owns the land and improvements of six (6) of its store locations, all of which are in Chicago, Milwaukee, Philadelphia and Chester, Pennsylvania. One of those locations, however, has been the subject of a condemnation proceeding. (See ITEM 1. BUSINESS and ITEM 5. PENDING LEGAL PROCEEDINGS.) Its subsidiary, Anbec, owns the land and improvements of one store location (in Chicago), which premises are leased to Associated for the latter's operation of a store. Associated leases its remaining store locations, for terms expiring on various dates through 1988. One store location is leased on a month-to-month basis. (See ITEM 5. PENDING LEGAL PROCEEDINGS.) The aggregate annual minimum rental paid by Associated during the fiscal year ended February 2, 1974 for the store locations which it leases was approximately $1,450,000. Certain of the leases, however, provide for the payment of additional rent based upon the volume of sales at the particular location, and for the payment by Associated of applicable real property taxes and/or other expenses.

Associated's executive, buying and administrative offices are located in a New York City warehouse (see ITEM 1. BUSINESS) leased by Associated for a term expiring in 1978. The warehouse has a floor area of approximately eighty thousand (80,000) square feet.

Fashion Outlet leases the premises upon which it operates its one retail store. Columbia has no independent operating offices and owns no facilities; all of Columbia's activities are conducted by Warren E. Buffett, its President and the Chairman of its Board of Directors, from his offices in Omaha, Nebraska.

ITEM 4. PARENTS AND SUBSIDIARIES.

A. Parents

As of February 2, 1974, Warren E. Buffett owned 39.9%* of the Company's common stock; First Manhattan Co. (of which David S. Gottesman was and is a general partner) held of record ten percent (10%) of that stock; Wheeler, Munger and Co. (of which Charles T. Munger was and is a general partner) owned ten percent (10%) of that stock; and Susan T. Buffett, the spouse of Warren E. Buffett, owned approximately three percent (3%) of that stock. (See ITEM 11. PRINCIPAL SECURITY HOLDERS AND SECURITY HOLDINGS OF MANAGEMENT and ITEM 12. DIRECTORS OF REGISTRANT.) First Manhattan Co. and Wheeler, Munger & Co. each disclaims any status which would cause it to be deemed a parent Company.

B. Subsidiaries

The Company owns one hundred percent (100%) of the issued and outstanding voting securities of its subsidiary, Associated Retail Store, Inc., an Illinois corporation. Associated owns one hundred percent (100%) of the issued and outstanding voting securities of its

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* This percentage was computed without taking into account Mr. Buffet's interest as trustee under various trust instruments in certain shares of the Company's common stock, and his interest in certain other shares of such stock as a result of the interest in those shares of a member of his family. See ITEM 11. PRINCIPAL SECURITY HOLDERS AND SECURITY HOLDINGS OF MANAGEMENT.

three subsidiaries: Anbec, Inc., an Illinois corporation; Columbia Insurance Company, a Nebraska corporation; and Fashion Outlet of Michigan, Inc., a Michigan corporation. Associated, Anbec and Fashion Outlet are included in the consolidated financial statements of the Company. In accordance with Rule 4.07 of Regulation S-X, promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, Columbia is not so consolidated.

As of February 2, 1974, the Company, Associated and Columbia in the aggregate beneficially owned approximately 16% of the common stock of Blue Chip Stamps (hereinafter referred to as "Blue Chip"), a California corporation, and Warren E. Buffett beneficially owned approximately 13% of that stock. On that date, the beneficial ownership of that stock by Mr. Buffett and his associates, including Associated, Columbia, National Indemnity, National Fire and Marine Insurance Company (a wholly-owned subsidiary of Berkshire), Cornhusker Casualty Company, Lakeland Fire and Casualty Company, Texas United Insurance Company and Home and Automobile Insurance Company (each of which is a wholly-owned subsidiary of National Indemnity) aggregated approximately 48% of the common stock of Blue Chip. In addition, Wheeler, Munger & Co. (of which Charles T. Munger is a general partner) owned beneficially on that date approximately ten percent (10%) of that stock, and David S. Gottesman, a general partner of First Manhattan Co., and members of his immediate family, and members of the immediate family of Charles F. Heider, owned beneficially less than one percent (1%) of that stock.

As of February 2, 1974, the Company, Associated and Columbia in the aggregate owned beneficially approximately 11% of the common stock of Berkshire, a Delaware corporation. In addition, on that date Warren E. Buffett and Susan T. Buffett, his spouse, respectively owned beneficially approximately 33.3% and approximately 2.5% of that stock.

ITEM 5. PENDING LEGAL PROCEEDINGS.

With the following exception, other than ordinary routine litigation incidental to the business of the Company, Associated and Associated's subsidiaries, none of the said companies are parties to any material pending legal proceedings and none of their property is the subject thereof.

Prior to May 1973, Associated owned the improved real property located at 913-917 Market Street, Philadelphia, Pennsylvania, where it operates one of its retail stores. Condemnation proceedings were instituted against that property by the Philadelphia Redevelopment Authority on May 21, 1970, in the Court of Common Pleas of Philadelphia County, in which proceedings Associated challenged the condemnation. Associated continued to occupy the premises and to operate the store thereon during the course of the condemnation proceedings, as it had since 1951.

During the proceedings, the Philadelphia Redevelopment Authority paid into court the sum of $1,348,095, representing the Authority's eatimate of what amount would constitute fair compensation to Associated for the condemnation. In May, 1973, Associated was paid that sum as proceeds of the condemnation and anticipates the receipt of an additional sum of $134,809.50 (for a total of $1,482,904.50) plus certain other consideration, in exchange for its agreement to withdraw its challenge of the condemnation. The formal consummation of the settlement has taken place. (See <u>ITEM 1. BUSINESS</u> and <u>ITEM 3. PROPERTIES</u>)

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* Associated has operated another of its stores on premises located at 835 Market Street, Philadelphia, Pennsylvania, which premises have been leased by Associated from the Philadelphia Redevelopment Authority on a month-to-month basis. The Authority took title to the real property and improvements at that location from Associated's former landlord prior to the beginning of the fiscal year ended February 3, 1973, following a condemnation proceeding in which Associated, as tenant, had challenged the condemnation. Associated's participation in that proceeding terminated prior to the beginning of the said fiscal year. (See <u>ITEM 1. BUSINESS</u> and <u>ITEM 3. PROPERTIES</u>.)

ITEM 6. INCREASES AND DECREASES IN OUTSTANDING SECURITIES.

None.

ITEM 7. APPROXIMATE NUMBER OF EQUITY SECURITY HOLDERS.

Title of class	Number of record holders (a)
Diversified Retailing Co., Inc., common stock, par value $0.0003 per share	288

ITEM 8. EXECUTIVE OFFICERS OF THE REGISTRANT.

Name	Age (a)	Office(s) held
Warren E. Buffett	43	Chairman of the Board of Directors
Robert M. Goldman (b)	57	President; Director
David S. Gottesman	47	Vice-President; Director
Charles T. Munger	50	Vice-President; Director
Charles F. Heider	47	Director
Max E. Blumenthal (b)	33	Secretary
Larry C. Cummings (b)	30	Treasurer; Assistant Secretary

ITEM 9. INDEMNIFICATION OF DIRECTORS AND OFFICERS.

The Company has no charter provision, by-law, contract or arrangement under or pursuant to which any of its Directors or Officers are insured or indemnified in any manner against any liability which may be incurred in their capacity as such. However, under article 23, section 64 of the Annotated Code of Maryland (1957 ed., as amended), the Company may indemnify any Director, Officer, employee or agent of the Company against any expenses or liability incurred as a result of his good faith performance of duty in such capacity, subject to certain restrictions upon such indemnification which are provided in the said statute.

(a) The information is given as of February 2, 1974.

(b) Both Mr. Goldman and Mr. Blumenthal are partners in the law firm of Frank, Bernstein, Conaway and Goldman, 1300 Mercantile Bank and Trust Building, 2 Hopkins Plaza, Baltimore, Maryland, which firm represents the Company. Mr. Cummings is an employee of that firm.

ITEM 10. FINANCIAL STATEMENTS AND EXHIBITS FILED.

A. Financial statements

A list of the financial statements and schedules of the Company, of Associated, and/or of Associated's subsidiaries which are filed herewith immediately precedes those documents herein.

B. Exhibits filed

Exhibit A: Computation of earnings per share

Exhibit B: 1974 Annual Report of Blue Chip Stamps

Exhibit C: 1973 Annual Report of Berkshire Hathaway, Inc.

C. The Company is furnishing to the Commission, at the time of filing its report on this form, four copies of a proxy statement and proxy sent to the stockholders of the Company in connection with the annual meeting of shareholders held on February 5, 1974. The Company will furnish to the Commission four copies of its Annual Report to the stockholders of the Company promptly upon its having been prepared and furnished to the said stockholders.

PART II

ITEM 11. PRINCIPAL SECURITY HOLDERS AND SECURITY HOLDINGS OF MANAGEMENT.

A. Principal Security Holders

Name and Address	Title of class	Type of ownership	Amount owned (a)	Percent of class
Warren E. Buffett 5505 Farnan Street Omaha, Nebraska 68131	common	record and beneficial	398,959 (b)	39.89%
First Manhattan Co. 30 Wall Street New York, New York 10005	common	record only	100,000 (c)	10.00%
Wheeler, Munger & Co. 618 South Spring St. Los Angeles, California 99914	common	record and beneficial	100,000 (d)	10.00%

(a) The information is given as of February 2, 1974.

(b) This amount does not include any of the following shares of common stock, as to which Mr. Buffett disclaims the beneficial ownership:

(i) 31,113 shares held by a member of Mr. Buffett's immediate family;

(ii) 3,732 shares held in trust under the Last Will and Testament of Howard H. Buffett, deceased, as to which Mr. Buffett is the trustee;

(iii) 552 shares held in equal amounts in three trusts, each of which is for the benefit of a member of Mr. Buffett's family, and as to each of which he is a co-trustee;

(iv) 2,304 shares held in three equal amounts by Mrs. Doris B. Lear, a sister of Mr. Buffett, as Custodian under the Nebraska Uniform Gifts to Minors Act, each for the benefit of a member of Mr. Buffett's family; and

(v) 429 shares held in equal amounts in three trusts, as to each of which Mr. Buffett is a co-trustee.

(c) As a general partner of First Manhattan Co., David S. Gottesman, a Director and a Vice-President of the Company, beneficially owned 35,000 of the said 100,000 shares. An additional 5,000 of the said 100,000 shares are held in trust for the benefit of certain members of Mr. Gottesman's immediate family and an additional 7,296 of the said 100,000 shares are owned beneficially by a member of Mr. Gottesman's immediate family. The remaining 52,704 of the said 100,000 shares are owned beneficially by other partners of the firm or their personal representatives. Mr. Gottesman disclaims the beneficial ownership of the shares held in the said trust and of the shares owned by the member of his immediate family.

(d) As a general partner of Wheeler, Munger & Co., Charles T. Munger, a Director and a Vice-President of the Company, possessed an interest in the said 100,000 shares.

B. Security Holdings of Management

Title of class	Amount beneficially owned (e)	Percent of class
Diversified Retailing Co., Inc., common stock, par value 0.0003 per share (f)	433,959 (g)	43.40%

Under the partnership agreement of First Manhattan Co., the firm possesses certain voting rights as to the 100,000 shares of the Company's common stock which the firm owns of record and which is beneficially owned in various amounts by certain partners therein, members of their immediate families or personal representatives. (See note (c) to this Item.)

(e) Subject to the exceptions indicated in note (g) to this Item, this column indicates the number of shares of the common stock of the Company beneficially owned directly or indirectly by all Directors and Officers of the Company, as a group, as of February 2, 1974.

(f) The Company has no other class of equity securities. No Director or Officer possesses the beneficial ownership of any share or shares of equity securities of the Company's subsidiary, Associated, or of any of Associated's subsidiaries (Anbec, Columbia and Fashion Outlet). As noted under ITEM 4. PARENTS AND SUBSIDIARIES, the Company, Associated and Columbia each disclaims control of Blue Chip.

(g) This amount does not include any of the following shares of common stock:

(i) the shares referred to in notes (b) and (d) to this Item, which notes are incorporated herein by reference;

(ii) The 5,000 shares held in trust for the benefit of certain members of David S. Gottesman's immediate family and the 7,296 shares owned beneficially by a member of Mr. Gottesman's immediate family referred to in note (c) to this Item, which note is incorporated herein by reference; and

(iii) 577 shares owned beneficially by a member of Charles C. Heider's immediate family, individually, and 370 shares owned beneficially by a member of Mr. Heider's immediate family as custodian for certain other members of Mr. Heider's immediate family, as to all of which shares Mr. Heider, a Director of the Company, disclaims the beneficial ownership.

(iv) 2,211 shares owned beneficially by M. Peter Moser, a partner in the law firm of Frank, Bernstein, Conaway & Goldman (in which Messrs. Goldman and Blumenthal are partners) or by members of Mr. Moser's immediate family.

ITEM 12. DIRECTORS OF THE REGISTRANT.

Each of the following persons served as a Director of the Company during the entire fiscal year ended February 2, 1974. The term of office of each such Director expired on February 5, 1974, the date upon which the Company held its annual meeting of stockholders. Each of the said persons was reelected for another full term as a Director, which term will expire on February 4, 1975.

A. Warren E. Buffett

Warren E. Buffett is the Chairman of the Board of Directors of the Company, having held that office since the Company's organization in 1966. Since January 1, 1970, Mr. Buffett's principal occupation has consisted of the making of personal investments. During the eight years prior thereto, his principal occupation was that of general partner of Buffett Partnership, Ltd. Since 1970, Mr. Buffett has been the Chairman of the Board of Directors of Associated and of Berkshire, and the Chairman of the Board of Directors, President and Treasurer of Columbia. Mr. Buffett is also the Chairman of the Board of Directors of Cornhusker Casualty Company and of National Fire and Marine Insurance Company.

B. David S. Gottesman

David S. Gottesman, a Director and a Vice-President of the Company, is and has been for the past five years a general partner in the broker-dealer securities firm of First Manhattan Co., a member of the New York Stock Exchange.

C. Charles T. Munger

Charles T. Munger, a Director and a Vice-President of the Company, is and has been for the past five years a general partner in the broker-dealer securities firm of Wheeler, Munger & Co., a member of the Pacific Coast Stock Exchange.

D. Charles F. Heider

Charles F. Heider, a Director of the Company, is and has been since 1970 the President of Chiles, Heider & Co. From 1966 to 1970, Mr. Heider was the Executive Vice-President of First Mid America, Inc. Each company is a broker-dealer securities firm and a member of the New York Stock Exchange.

E. Robert M. Goldman

Robert M. Goldman, a Director and the President of the Company, is and has been since July 1, 1966, a partner of the Maryland law firm of Frank, Bernstein, Conaway & Goldman. For more than fifteen years prior thereto, Mr. Goldman had been a partner in the Maryland law firm of Nyburg, Goldman and Walter, which on the said date was merged into the firm of Frank, Bernstein, Conaway & Goldman.

ITEM 13. REMUNERATION OF DIRECTORS AND OFFICERS.

Name of individual or number of persons in group	Capacities in which remuneration was received	Aggregate direct remuneration (a)
Larry C. Cummings	Treasurer	$500.00
All seven Directors and Officers as a group		500.00

ITEM 14. OPTIONS GRANTED TO MANAGEMENT TO PURCHASE SECURITIES.

None.

ITEM 15. INTEREST OF MANAGEMENT AND OTHERS IN CERTAIN TRANSACTIONS.

A. Other than the following, there have been no transactions

(a) Subject to the exceptions indicated in note (c) to this Item, this column indicates the aggregate amount of direct remuneration paid by the Company, Associated and Associated's subsidiaries to the person or persons specified, in all capacities, during the Company's fiscal year ended February 2, 1974.

(b) This amount does not include legal fees in the amount of $15,364.00 which the Company accrued during its fiscal year ended February 2, 1974, to the law firm of Frank, Bernstein, Conaway & Goldman, in which Messrs. Goldman and Blumenthal are and were at the time of such payment partners. Nor does the said amount include any additional such legal fees incurred by the Company between January 1, 1974, and February 2, 1974, for which amounts the said firm had not billed the Company as of February 2, 1974. Nor does the said amount include the interest of David S. Gottesman, as a partner in First Manhattan Co., in certain commissions paid to First Manhattan Co. by one of Associated's subsidiaries. See ITEM 15. INTEREST OF MANAGEMENT AND OTHERS IN CERTAIN TRANSACTIONS.

since the beginning of the fiscal year ended February 2, 1974, nor are there any presently proposed transactions, to which the Company, Associated or any of Associated's subsidiaries was or is to be a party, in which any Director or Officer of the Company, or any security holder named under section A of Item 11 hereof, or any relative or spouse of any of the foregoing persons who has the same home as such person or who is a Director or Officer of the Company or of Associated or any of Associated's subsidiaries, had or is to have a direct or indirect material interest:*

(1) During the Company's fiscal year ended February 2, 1974, Columbia purchased and sold certain securities traded on the New York Stock exchange. Those transactions were made through First Manhattan Co., of which David S. Gottesman is a general partner, acting as broker for Reinsurance Corp. of Nebraska. The commissions paid to First Manhattan Co. in connection with the said purchases were determined by the application of the prevailing commission rates and totaled approximately $4,652.00.

(2) During the Company's fiscal year ended February 2, 1974, Columbia accepted reinsurance contracts from National Indemnity, of which Warren E. Buffett is the Chairman of the Board of Directors, representing premiums written in the approximate amount of $2,161,947.00. National Indemnity is paid ceding commissions equal to approximately one-half of the standard commissions. (See ITEM 1. BUSINESS.) The commissions paid by Columbia to National Indemnity aggregated approximately $528,148.00 during the calendar year 1973. (The records of both companies are kept on a calendar year accrual basis.)

(3) During the Company's fiscal year ended February 2, 1974, the Company paid and/or incurred certain legal fees in connection

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*Mr. Benjamin F. Rosner, the President of Associated (but neither an Officer nor a Director of the Company), owns and leases to Associated the land and improvements upon which Associated operates one of its retail stores.

with the representation of the Company by the law firm of Frank, Bernstein, Conaway & Goldman. (See note (b) to ITEM 13. REMUNERATION OF DIRECTORS AND OFFICERS.)

(4) On March 15, 1974, the Directors of the Company approved in principal the proposed merger of the Company with and into Berkshire. The Company with its subsidiaries owns 11.2% of the outstanding capital stock of Berkshire. Warren E. Buffett, a Director of the Company owning more than ten percent (10%) of the issued and outstanding stock of the Company, is also a Director of Berkshire and owns more than ten percent (10%) of the issued and outstanding stock of Berkshire. A registration statement on Form S-14 will be filed by Berkshire in connection with the proposed merger. (See ITEM 4. PARENTS AND SUBSIDIARIES and ITEM 11. PRINCIPAL SECURITY HOLDERS AND SECURITY HOLDINGS OF MANAGEMENT).

B. During the Company's fiscal year ended February 2, 1974, no Director or Officer of the Company or associate of such persons was indebted to the Company, Associated or any of Associated's subsidiaries.

C. Other than any payments which may have been made pursuant to the terms of any pension, retirement, savings or similar plan which may have been provided by the Company, Associated or any of Associated's subsidiaries, during the Company's fiscal year ended February 2, 1974, there were no transactions, and there is no presently proposed transaction, to which any of the said plans was or is to be a party, in which any Director or Officer of the Company, any security holder named under section A of Item 11 hereof, or any relative or spouse thereof or relative of any such spouse who has the same home as any such Director, Officer or security holder or who is a Director or Officer of Associated or any of Associated's subsidiaries, had or is to have a direct or indirect material interest.

* * * * * * * * * * *

Pursuant to the requirements of Section 13 or 15(d) 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.

DIVERSIFIED RETAILING COMPANY, INC.

By: Robert M. Goldman

Robert M. Goldman, President

Date: May 3, 1974

ANNUAL REPORT ON FORM 10-K

ITEM 10(a)

FINANCIAL STATEMENTS AND SCHEDULES

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

The following consolidated financial statements and schedules of the registrant and its subsidiary and of the registrant (parent company) for the fiscal years 1974 and 1973 are submitted herewith:

Consolidated:
- Consolidated Balance Sheet
- Consolidated Statement of Earnings
- Consolidated Statement of Retained Earnings
- Consolidated Statement of Changes in Financial Position
- Notes to Consolidated Financial Statements

Parent Company only:
- Balance Sheet
- Statement of Earnings
- Statement of Retained Earnings
- Statement of Changes in Financial Position
- Notes to Financial Statements

Schedule III - Investments in Securities of Affiliates
Schedule V - Property, Plant and Equipment
Schedule VI - Accumulated Depreciation, Depletion and Amortization of Property, Plant and Equipment
Schedule XVI - Supplementary Income Statement Information

All other schedules (Nos. I, II, IV, VII, VIII, IX, X, XI, XII, XIII, XIV, XV, XVII, XVIII and XIX) for which provision is made in the applicable regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted. With respect to Schedule XIII, the information applicable to the consolidated subsidiaries has been omitted as they are wholly-owned and the answers to Column G would be "none".

The following financial statements and schedules of the unconsolidated insurance subsidiary for the years 1973 and 1972 are submitted herewith:

Balance Sheet
Statement of Earnings
Statement of Capital Stock and Surplus
Statement of Changes in Financial Position
Notes to Financial Statements
Schedule I - Bonds
Schedule II - Stocks - Other Than Stocks of Affiliates
Schedule V - Summary of Investments in Securities - Other Than Securities of Affiliates
Schedule VI - Investments in Stocks of Affiliates
Schedule VII - Premiums, Losses and Underwriting Expenses
Schedule X - Income from Dividends - Equity in Net Profit of Affiliates
Schedule XI - Summary of Realized Gain (Losses) on Sale or Maturity of Investments

All other schedules (Nos. III, IV, VIII and IX) for which provision is made in the applicable regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted. The information required in Schedule VIII is included in the notes to the financial statements of the insurance subsidiary.

The following exhibits are attached and made a part of this filing:

Exhibit A - Computation of Earnings Per Share
Exhibit B - Annual Report of Blue Chip Stamps - March 2, 1974
Exhibit C - Annual Report of Berkshire Hathaway Inc. - December 29, 1973

ERNST & ERNST

ONE NORTH CHARLES

BALTIMORE, MARYLAND

21201

Board of Directors
Diversified Retailing Company, Inc.
Baltimore, Maryland

We have examined the financial statements of Diversified Retailing Company, Inc. (parent company) and the consolidated financial statements of Diversified Retailing Company, Inc. and subsidiary for the years ended February 2, 1974 and February 3, 1973, and the related schedules listed in the accompanying index. 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. The consolidated financial statements include the equity in earnings of an unconsolidated subsidiary and certain affiliated companies. The financial statements of these companies used as the basis of recording such equity in earnings were examined by other auditors whose reports were furnished to us. Our opinion expressed herein, insofar as it relates to the amount of income included for those companies for each of the years ended February 2, 1974 and February 3, 1973, is based solely on the reports of other auditors.

The report of the other auditors on the financial statements of Blue Chip Stamps (Blue Chip), an affiliated company, is qualified with respect to the resolution of pending legal proceedings referred to in Note 11 to the financial statements of Blue Chip, which statements are included as Exhibit B to this annual report on Form 10-K. The investment in Blue Chip is held by Associated and its unconsolidated subsidiary and is carried at cost plus equity in undistributed earnings, which at February 2, 1974 aggregated $12,491,000.

In our opinion, based upon our examination and the aforementioned reports of other auditors and subject to the effect, if any, on the financial statements resulting from the ultimate outcome of the legal proceedings referred to in the preceding paragraph, the accompanying balance sheets and statements of earnings, retained earnings and changes in financial position present fairly the financial position of Diversified Retailing Company, Inc. (parent company) and of Diversified Retailing Company, Inc. and subsidiary at February 2, 1974 and February 3, 1973, and the respective results of their operations, and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis. Further, it is our opinion that Schedules III (subject to the effect of the aforementioned legal proceedings), V, VI and XVI present fairly the information set forth therein.

ERNST & ERNST

Baltimore, Maryland
April 17, 1974

CONSOLIDATED BALANCE SHEET

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	February 2, 1974	February 3, 1973
ASSETS		
CURRENT ASSETS		
Cash	$ 2,504,058	$ 882,020
Short-term commercial paper and other marketable securities - at cost, which approximates market		1,495,297
Accounts receivable	420,159	249,212
Merchandise inventories - Note A	4,313,442	3,818,520
Prepaid expenses	79,026	74,195
TOTAL CURRENT ASSETS	7,316,685	6,519,244
INVESTMENTS AND OTHER ASSETS		
Investment in unconsolidated subsidiary - Notes A and B	8,429,055	7,516,244
Investment in affiliated companies - Notes A, C and D		
Berkshire Hathaway Inc.	5,227,024	2,924,157
Blue Chip Stamps	8,820,555	8,335,047
Other security investments - at cost		206,763
Other assets - Note A	381,094	598,111
	22,857,728	19,580,322
PROPERTY, PLANT AND EQUIPMENT - at cost, less allowance for depreciation and amortization of $645,525 and $991,852 - Notes A, E and K	921,594	1,756,340
	$31,096,007	$27,855,906

	February 2, 1974	February 3, 1973
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Trade and sundry accounts payable	$ 618,524	$ 388,027
Salaries, wages and bonuses	155,701	142,215
Taxes other than taxes on income	237,059	261,947
Accrued interest	161,476	162,008
Taxes on income	389,130	353,779
Other current liabilities	115,065	83,889
TOTAL CURRENT LIABILITIES	1,676,955	1,391,865
DEFERRED INCOME TAXES - Notes A, C, D and F	247,233	143,346
LONG-TERM DEBT - Note G		
8% Debentures due November 1, 1985	6,600,000	6,600,000
9% Notes payable	1,242,885	1,242,885
DEFERRED CREDIT - unamortized excess of carrying amount of net assets of subsidiary over acquisition cost - Note A	426,185	557,315
STOCKHOLDERS' EQUITY - Notes G and H		
Common Stock - voting, par value: $.0003		
Authorized: 3,333,333-1/3 shares		
Issued and outstanding: 1,000,000 shares	300	300
Additional paid-in capital	5,999,700	5,999,700
Retained earnings	14,902,749	11,920,495
	20,902,749	17,920,495
COMMITMENTS AND CONTINGENT LIABILITIES - Notes I and J		
	$31,096,007	$27,855,906

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973 (53 weeks)
Net sales (including leased department sales)	$38,398,636	$38,918,071
Cost of goods sold	25,023,201	25,427,906
	13,375,435	13,490,165
Selling, general and administrative expenses	12,165,363	11,775,923
	1,210,072	1,714,242
Other income and (deductions):		
Amortization of excess of net assets of subsidiaries over acquisition cost - Note A	131,130	131,130
Dividends	7,164	20,060
Interest and financing cost	(720,066)	(687,408)
Interest income	66,426	9,995
Miscellaneous	214,422	73,710
EARNINGS BEFORE INCOME TAXES, EQUITIES IN EARNINGS OF UNCONSOLIDATED SUBSIDIARY AND AFFILIATED COMPANIES AND EXTRAORDINARY ITEMS	909,148	1,261,729
Taxes on income:		
Federal - Notes A and F	287,500	410,000
State and local	139,000	255,000
	426,500	665,000
EARNINGS BEFORE EQUITIES IN EARNINGS OF UNCONSOLIDATED SUBSIDIARY AND AFFILIATED COMPANIES AND EXTRAORDINARY ITEMS	482,648	596,729
Equity in earnings of unconsolidated subsidiary - Note B	912,811	954,844
Equity in earnings of affiliated companies (net of deferred income taxes: 1974 - $114,115; 1973 - $83,628) - Notes A, C and D:		
Berkshire Hathaway Inc.	629,709	454,453
Blue Chip Stamps	561,508	718,995
	1,191,217	1,173,448
EARNINGS BEFORE EXTRAORDINARY ITEMS	2,586,676	2,725,021
Extraordinary items - Note K	395,578	193,021
NET EARNINGS	$ 2,982,254	$ 2,918,042

CONSOLIDATED STATEMENT OF EARNINGS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973 (53 weeks)
Earnings per share:		
Earnings before equities in earnings of unconsolidated subsidiary and affiliated companies and extraordinary items	$ .48	$ .60
Equity in earnings of unconsolidated subsidiary	.91	.96
Equity in earnings of affiliated companies	1.19	1.17
Extraordinary items	.40	.19
Net earnings	$ 2.98	$ 2.92

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973
Balance at beginning of year	$11,920,495	$ 9,002,453
Net earnings for the year	2,982,254	2,918,042
BALANCE AT END OF YEAR	$14,902,749	$11,920,495

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973
SOURCE OF FUNDS		
From operations:		
Net earnings before extraordinary items	$2,586,676	$2,725,021
Charges (credits) to earnings which did not affect working capital:		
Depreciation and amortization	145,531	176,472
Amortization of excess of carrying amount of net assets of subsidiary over acquisition costs	(131,130)	(131,130)
Deferred income taxes		(50,000)
Amortization of finance costs	28,202	28,202
Equity in earnings of unconsolidated insurance subsidiary	(912,811)	(954,844)
Equity in earnings of affiliated companies in excess of dividends received	(1,173,504)	(1,125,020)
Deferred taxes (related to equity in earnings of affiliated companies)	114,115	83,628
TOTAL FROM OPERATIONS	657,079	752,329
Extraordinary items:		
Income taxes applicable to extraordinary gain on exchange of securities		(82,724)
Proceeds from condemnation of property, net of income taxes	1,269,904	
Proceeds from long-term borrowing		51,341
Deductions from property, plant and equipment	7,013	1,827
Decrease in other assets	188,815	56,519
Decrease in other securities	206,763	
	2,329,574	779,292
APPLICATION OF FUNDS		
Investment in affiliated companies	1,625,099	943,099
Additions to property, plant and equipment	192,124	48,946
	1,817,223	992,045
INCREASE (DECREASE) IN WORKING CAPITAL	$ 512,351	($ 212,753)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

	1974	1973
INCREASE (DECREASE) IN COMPONENTS OF WORKING CAPITAL		
Current assets:		
Cash	$1,622,038	$ 7,815
Short-term commercial paper and other marketable securities	(1,495,297)	496,019
Accounts receivable	170,947	30,588
Merchandise inventories	494,922	(665,864)
Prepaid expenses	4,831	(107,084)
	797,441	(238,526)
Current liabilities:		
Trade and sundry accounts	230,497	(222,357)
Salaries, wages and bonuses	13,486	(17,786)
Taxes other than taxes on income	(24,888)	68,107
Accrued interest	(532)	4,663
Taxes on income	35,351	147,726
Other current liabilities	31,176	(6,125)
	285,090	(25,773)
NET CHANGE	$ 512,351	($212,753)

( ) indicate red figure.

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note A - SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

Diversified Retailing Company, Inc. is a holding company and has no operations. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Associated Retail Stores, Inc. (Associated). Intercompany accounts and transactions have been eliminated in consolidation.

Investment in Consolidated Subsidiary

At the date of acquisition of Associated by the Company, the carrying amount of the net assets of Associated was in excess of the Company's investment. Such excess amounted to $1,311,309 and is being amortized to income over a ten-year period. The unamortized balance is shown as a deferred credit in the balance sheet.

Investment in Unconsolidated Subsidiary

Columbia Insurance Company (formerly Reinsurance Corp. of Nebraska) was formed in 1970 as a wholly-owned unconsolidated subsidiary of Associated. Columbia maintains its records on a calendar-year basis in accordance with state insurance regulations; Associated uses the equity method to recognize its interest in the earnings of Columbia for the calendar periods ending within the fiscal periods of Associated ending one month thereafter.

Investments in Affiliated Companies

The Company and its subsidiaries hold common stock investments in Berkshire Hathaway Inc. and Blue Chip Stamps, which two companies are considered "investees" under the provisions of Accounting Principles Board Opinion No. 18. Accordingly, the Company uses the equity method of accounting for these investments, under which method the Company currently recognizes its proportionate share of earnings reported by those companies, net of deferred income taxes provided for under the assumption that such earnings will ultimately be distributed as taxable dividends. Provision is also made for amortization of the difference between cost of the investments and the underlying equity in net assets at the dates of acquisition; this provision, through the fiscal year ended February 3, 1973, was computed on the basis of a forty-year amortization period. With respect to the investment in Blue Chip Stamps, effective for the year ending February 2, 1974, the period of amortization of excess cost was reduced to seven remaining years from the beginning of the current fiscal year. This change has the effect of reducing income for the year ending February 2, 1974 by $363,000 ($0.36 per share). In the opinion of management, this change was necessary because of the anticipated continuing decline in the stamp operation of Blue Chip Stamps to which the excess cost originally related.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note A - (Cont'd) Blue Chip Stamps' fiscal year ends one month after that of the Company; the Company has not recognized this difference in its annual accounting for equity in earnings of Blue Chip, having recorded its equity in earnings of Blue Chip's year ending on or about February 28 in its year ending on or about the preceding January 31.

At February 2, 1974 and February 3, 1973 the Company, Associated and Columbia held in the aggregate 16% of the outstanding common stock of Blue Chip Stamps. At February 2, 1974 the companies held 11% and at February 3, 1973 9% of the outstanding stock of Berkshire Hathaway Inc. In addition certain related persons own 32% of Blue Chip Stamps and 36% of Berkshire Hathaway outstanding common stock. Disposition of all or any lesser amount of said common stock of these affiliated companies may be subject to certain restrictions. Trading in Berkshire common stock is not extensive, although trades have been executed between $70 and $80 per share. A representative fair market value of $75 would cause the holdings of the Company, Associated and Columbia to approximate $8,366,000. The National Association of Insurance Commissioners Valuation Committee has assigned a valuation of $7.25 per share to the stock of Blue Chip Stamps. Accordingly, on this basis, the "market" value of Associated's and Columbia's investments in Blue Chip Stamps approximates $6,104,000. The Company believes that while such valuations may be indicative of the value in the public market for a moderate number of shares, they are not necessarily indicative of the fair market value of the substantial blocks of shares held in Berkshire and Blue Chip.

The latest Annual Reports for Blue Chip Stamps and Berkshire Hathaway Inc. are included with this filing as exhibits B and C, respectively, and should be read in conjunction with the consolidated financial statements.

Accounts Receivable

In the opinion of management, no allowance for doubtful accounts is necessary due to the nature (primarily lay-away accounts) of the accounts receivable.

Merchandise Inventories

Inventories are determined by the first-in, first-out method and are priced at the lower of cost or market by use of the retail inventory method, except as to warehouse inventories which are priced at cost.

Property and Equipment

Expenditures for maintenance, repairs, renewals and betterments which represent improvements to property and equipment are capitalized; other such items are charged to current operations. At the time assets are retired or otherwise disposed of, the cost and related allowance for depreciation are eliminated from the asset and allowance accounts and any profit or loss on disposition is reflected in current operations. When assets become fully depreciated, the cost and related allowance for depreciation are written off.

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note A - (Cont'd) Depreciation for both financial accounting and income tax purposes is based on the 150% declining balance method as to buildings and on the straight-line method for substantially all other property and equipment.

Federal Income Taxes

The Company, Associated and Columbia file a consolidated Federal income tax return. The investment tax credit, not material in amount, is accounted for by the flow-through method.

Financing Costs

Certain costs incurred in connection with the issuance by the Company of its 8% Debentures have been capitalized in Other Assets and are being ratably amortized over the stipulated life of the debentures.

Note B - INVESTMENT IN UNCONSOLIDATED SUBSIDIARY

Associated owns all of the issued and outstanding capital stock of Columbia Insurance Company, which reinsures risks other than life and title. The carrying value of the investment represents cost plus equity in earnings as follows:

Payment for stock and contributions to capital:	
Cash	$2,500,000
Marketable securities	3,355,389
	5,855,389
Net earnings to December 31, 1972	1,660,855
BALANCE FEBRUARY 3, 1973	7,516,244
Net earnings for the year ended February 2, 1974	912,811
BALANCE FEBRUARY 2, 1974	$8,429,055

Note C - INVESTMENT IN BERKSHIRE HATHAWAY INC.

The carrying value of the investment in common stock of Berkshire Hathaway Inc. represents the purchase cost of the shares plus equity in post-acquisition earnings, adjusted for amortization, on a forty-year basis, of the difference between purchase cost and underlying net asset values at dates of acquisition. This is summarized as follows:

	February 3, 1973	February 2, 1974
Shares owned	41,745	60,836

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note C - (Cont'd)

	February 3, 1973	February 2, 1974
Purchase cost:		
Representing underlying net asset values at dates of acquisition	$2,200,280	$3,630,277
Cumulative excess of cost over equity in net assets on Associated's investment, net of amortization for fiscal years 1973 and 1974 of $370 and $6,716, respectively	157,651	346,407
Cumulative excess of equity in net assets over cost on Diversified's investment, net of amortization for fiscal years 1973 and 1974 of $11,236 and $14,533, respectively	(136,882)	(133,585)
	20,769	212,822
Equity in post-acquisition earnings	703,108	1,383,925
CARRYING AMOUNT	$2,924,157	$5,227,024

The cost of Associated's investment in Berkshire Hathaway Inc. exceeded the underlying equity in net assets at the dates of acquisition of the several blocks of stock by $353,123 at February 2, 1974 and $158,021 at February 3, 1973. The cost of the Company's investment in Berkshire was less than the underlying equity in net assets at the dates of acquisition of the several blockssof stock by $148,118 at both February 2, 1974 and February 3,11973. Berkshire has paid no dividends during the period of affiliation.

Deferred income taxes of approximately $99,000 at February 2, 1974 and $51,000 at February 3, 1973 have been provided with respect to the equity in post-acquisition earnings, assuming their ultimate distribution as a taxable dividend.

Columbia Insurance Company has an additional investment in 48,715 shares of Berkshire Hathaway Inc.

Note D - INVESTMENT IN BLUE CHIP STAMPS

The carrying value of the investment in 591,900 shares of common stock of Blue Chip Stamps represents the purchase cost, less amortization of the excess of cost over net value of underlying assets at dates of acquisition plus equity in undistributed post-acquisition earnings, as follows:

Note D -
(Cont'd)

	February 3, 1973	February 2, 1974
Purchase cost:		
Representing underlying net asset values at dates of acquisition	$5,075,471	$5,075,471
Cumulative excess of cost over equity in net assets, net of amortization for fiscal years 1973 and 1974 of $137,260 and $427,141, respectively	1,971,765	1,681,884
	7,047,236	6,757,355
Equity in post-acquisition undistributed earnings	1,287,811	2,063,200
CARRYING AMOUNT	$8,335,047	$8,820,555

The cost of Associated's investment in Blue Chip (Diversified has no investment in Blue Chip) exceeded the underlying equity in net assets at the dates of acquisition of the several blocks of Blue Chip stock by $2,109,025 at February 2, 1974 and February 3, 1973. Blue Chip dividends received by Associated were $142,056 for both fiscal years ended February 2, 1974 and February 3, 1973 and have been applied as a reduction of the investment in the affiliated company in accordance with the equity method of accounting for such investments as described in Note A.

Through February 3, 1973 the excess of cost over underlying net asset values was being written off over a forty-year period. Commencing with the current fiscal year, this period of amortization was reduced to seven remaining years from February 4, 1973.

Deferred income taxes of approximately $149,000 at February 2, 1974 and $92,000 at February 3, 1973 have been provided with respect to the equity in post-acquisition undistributed earnings, assuming their ultimate distribution as a taxable dividend.

Columbia Insurance Company has an additional investment of 250,000 shares of Blue Chip Stamps.

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note E - PROPERTY AND EQUIPMENT

Property and equipment are comprised of the following:

	February 2, 1974	February 3, 1973
Land	$ 201,515	$ 894,722
Buildings	210,197	599,373
Building improvements	156,095	154,880
Leasehold improvements	352,913	351,805
Furniture, fixtures and equipment	646,399	747,412
	1,567,119	2,748,192
Less allowances for depreciation and amortization	645,525	991,852
	$ 921,594	$1,756,340

Generally, the estimated useful lives used for computing depreciation range from 20 to 33 years for buildings, 4 to 14 years for furniture, fixtures and equipment and the life of the lease for leasehold improvements.

See Note K regarding the condemnation of certain property during the year ended February 2, 1974.

Note F - INCOME TAXES

Federal income tax returns of the Company and its subsidiaries have been examined and deficiencies assessed have been paid for years through February 1, 1969.

The reasons for the difference in 1974 between tax expense on ordinary income and the amount computed by applying the statutory federal income tax rate of 48% were as follows:

Earnings before income taxes, equities and extraordinary items	$909,148
Less state taxes	(139,000)
	770,148
Statutory rate	48%
	370,000
Effect of:	
Capital gains rates on securities gain included in miscellaneous income	(20,500)
Non-taxable income arising from amortization of excess of net assets of subsidiaries over acquisition cost	(62,000)
TOTAL TAX EXPENSE	$287,500
Effective rate	37.3%

Note G - DEBT

Under a line of credit arrangement for short-term debt, Associated may borrow up to $4,000,000 on such terms as it and the bank may mutually agree upon. The line of credit can be withdrawn at the bank's option. There were no compensating balance arrangements under the line of credit nor any outstanding borrowings at any month-end during the year ended February 2, 1974, although the line was used for brief periods on a few occasions during the year.

Interest and financing costs reflected in the consolidated statements of earnings relate principally to long-term debt.

8% Debentures

The debentures were issued under a trust indenture dated November 1, 1967, under which the aggregate principal amount which may be issued is unlimited, the debentures are not secured by any lien, and there are no restrictions against secured or unsecured borrowings of the Company. They bear interest at a fixed annual rate of 8% payable semi-annually and bear participating additional interest each year up to a maximum of 1% contingent upon the amount of adjusted consolidated earnings before income taxes, as defined, for the previous fiscal year. No contingent interest was payable under these provisions during the last two fiscal years.

The debentures are subject to redemption at the option of the Company at 105% of par plus accrued interest to October 31, 1974 and thereafter at percentages reducing to 100% at November 1, 1983. The debentures are also contingently subject to redemption at par plus accrued interest through operation of a sinking fund. If the adjusted consolidated net worth, as defined, of the Company is less than $12 million, sinking fund payments are generally required. No such contingent sinking fund payments have been required and none appear imminent.

The debentures are further subject to redemption at the option of each debenture holder, exercisable within 60 days following notice that, other than by reason of the death of Warren E. Buffett, said Warren E. Buffett or an organization controlled by him, shall cease to own in combined holdings a larger block of shares with voting rights of the Company than any other stockholder, or combination of stockholders, controlled by a single individual.

The Articles of Incorporation of the Company provide that if and as long as an Event of Default exists or the Adjusted Consolidated Net Worth of the Company is less than $8,000,000, and either condition continues for a period of thirty days, then the holders of the Debentures, to the exclusion of the holders of the Company's stock, shall be entitled to vote (i) to elect directors of the Company, and (ii) to approve the sale, lease or other disposition of all or

Note G - (Cont'd) substantially all of the assets of the Company and distribution of the proceeds thereof to the extent necessary to pay all sums due Debenture holders and other creditors. No amendment to such provisions shall be made as long as any Debentures are outstanding without the written approval of the holders of two-thirds in principal amount of the Debentures then outstanding. If there are such voting rights, each holder of the Debentures will have one vote for each $1,000 principal amount of Debentures.

The Trust Indenture covering the Debentures contains certain restrictions applicable to the Company relating to net worth, redemption of stock and payment of dividends. Retained earnings of approximately $640,000 were subject to such restrictions at February 2, 1974.

9% Notes Payable

The Notes Payable represent purchase obligations for shares of Berkshire Hathaway Inc. acquired at various dates. These notes become due at varying dates drom May 1, 1974 to January 4, 1988 and bear interest at 9% per year, payable semi-annually. The notes are also due on the respective payees' demand on or after the expiration of twelve months following the date of death of Warren E. Buffett.

Principal payments due on these notes are summarized by fiscal year as follows:

1975-76	$ 3,731
1977	109,731
1978-81	3,731
1982	357,969
1983	571,299
1986-87	26,500
1988	128,500

The principal amount maturing within one year has not been classified as a current liability.

Note H - STOCKHOLDERS' EQUITY

There were no changes in the capital stock and additional paid-in capital accounts during the fiscal years ended February 2, 1974 and February 3, 1973.

At February 2, 1974 retained earnings included $5,354,000 representing undistributed earnings of affiliated companies and Associated's unconsolidated subsidiary as follows: Berkshire Hathaway - $1,293,000; Blue Chip - $1,487,000; and Columbia - $2,574,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

February 2, 1974 and February 3, 1973

Note I - LEASES

Associated and its consolidated subsidiaries lease 68 stores, warehouse facilities and New York offices, under leases expiring at various dates through 1988. The leases require minimum annual rental plus, under the terms of certain leases, additional payments for taxes, other expenses and percentage rentals. The amount of total rental expense and contingent rentals included in the statements of earnings is as follows:

	Rental Expense	Contingent Rentals
Fiscal year ended:		
1973	$1,772,000	$189,000
1974	1,844,000	229,000

Associated also has leased and leases data processing equipment for approximately $53,000 a year through 1975. The present value of noncapitalized financing leases is not material. Likewise the impact on net income if such leases had been capitalized would not be material.

Minimum annual rental obligations under existing real estate leases were as follows at February 2, 1974:

Fiscal year ending:	
1975	$1,452,000
1976	1,237,000
1977	1,126,000
1978	840,000
1979	495,000
1980-1984	1,627,000
1985-1988	348,000
TOTAL	$7,125,000

Note J - PENSION PLAN

Associated has a non-contributory trusteed pension plan covering eligible full-time employees. The total pension expense for each fiscal year approximates $65,000 which includes amortization of past service liability over a thirty-year period. Associated's policy is to fund pension cost accrued.

Participants do not have a vested interest in the plan. The unfunded past service liability at February 2, 1974 was approximately $40,000.

Note K - EXTRAORDINARY ITEMS

Year ended February 3, 1973 - $193,021 Extraordinary Gain

In March 1972 the Company exchanged certain investment securities for 300,000 shares of Blue Chip Stamps common stock with a basis of $3,861,000. This transaction was considered a taxable exchange under applicable income tax regulations and the gain on the exchange of $193,021, after reduction for income taxes of $82,724, has been shown as an extraordinary gain in the statement of earnings.

Year ended February 2, 1974 - $395,578 Extraordinary Gain

In May 1973 Associated Retail Stores, Inc. received condemnation proceeds of approximately $1,348,000 for certain real estate and improvements which were reflected on the books at $874,000, net of depreciation allowance. In the opinion of legal counsel, an additional $135,000 will be realized from this proceeding; accordingly, the latter amount has been recognized in computing gain of $395,578 net of $213,000 applicable income taxes, reflected as an extraordinary item in the statement of earnings for the year ended February 2, 1974.

Note L - PROPOSED MERGER

The Board of Directors of the Company has approved for submission to the shareholders a proposal to merge the Company into Berkshire Hathaway Inc., an affiliate (see Notes A and C). Consummation of the merger is subject to a number of conditions, including the approval of certain regulatory authorities and a favorable stockholders' vote on the part of each corporation. Shares of Berkshire Hathaway Inc. are proposed to be issued to the Company's stockholders in exchange for their holdings in the Company in this transaction.

Note M - SUPPLEMENTAL NOTE - INVENTORIES

Inventories used in the computation of cost of goods sold were as follows:

January 29, 1972	$4,484,384
February 3, 1973	3,818,520
February 2, 1974	4,313,442

Note N - 52-53 WEEK YEARS

The Company's and Associated's fiscal year ends on the Saturday nearest January 31. The fiscal year ended February 2, 1974 and February 3, 1973 comprised 52 and 53 weeks, respectively.

BALANCE SHEET

DIVERSIFIED RETAILING COMPANY, INC.

	February 2, 1974	February 3, 1973
ASSETS		
Cash	$ 75,304	$ 83,992
Due from subsidiary		21,000
Note receivable from subsidiary	6,600,000	
Investment in subsidiary - Notes A and B	20,394,648	24,357,260
Investment in affiliated company - Notes A and C	2,057,356	1,707,532
Unamortized cost of long-term financing - Note A	331,071	359,273
	$29,458,379	$26,529,057
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accrued interest and other expenses	$ 179,703	$ 171,610
Due to subsidiary	46,115	
Deferred income taxes - Note A	60,742	36,752
8% Debentures - Note D	6,600,000	6,600,000
9% Notes payable - Note D	1,242,885	1,242,885
Unamortized excess of carrying amount of net assets of subsidiary over acquisition cost - Note A	426,185	557,315
Stockholders' equity - Notes D and F:		
Common Stock - voting, par value $.0003		
Authorized: 3,333,333-1/3 shares		
Issued and outstanding: 1,000,000 shares	300	300
Additional paid-in capital	5,999,700	5,999,700
Retained earnings	14,902,749	11,920,495
	20,902,749	17,920,495
	$29,458,379	$26,529,057

See notes to financial statements.

STATEMENT OF EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973 (53 weeks)
Income:		
Interest from subsidiary	$ 487,385	
Amortization of excess of net assets of subsidiary over acquisition cost - Note A	131,130	$ 131,130
	618,515	131,130
Expenses:		
General and administrative expenses	34,837	19,978
Interest and financing costs - Note A	668,146	667,470
	702,983	687,448
LOSS BEFORE INCOME TAXES, EQUITIES IN EARNINGS OF SUBSIDIARY AND AFFILIATED COMPANY	(84,468)	(556,318)
Federal income tax credit - Note A	103,500	330,000
INCOME (LOSS) BEFORE EQUITIES IN EARNINGS OF SUBSIDIARY AND AFFILIATED COMPANY	19,032	(226,318)
Equity in earnings of subsidiary - Notes A and B	2,637,388	2,840,255
Equity in earnings of affiliated company net of deferred income taxes: 1974 - $23,990; 1973 - $23,261 - Notes A and C	325,834	304,105
NET EARNINGS	$2,982,254	$2,918,042
Earnings per share:		
Income (loss) before equities in earnings of subsidiary and affiliated company	$ .02	($ .23)
Equity in earnings of subsidiary	2.64	2.84
Equity in earnings of affiliated company	.32	.31
Net earnings	$ 2.98	$ 2.92

See notes to financial statements.

STATEMENT OF RETAINED EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973
Balance at beginning of year	$11,920,495	$ 9,002,453
Net earnings for the year	2,982,254	2,918,042
BALANCE AT END OF YEAR	$14,902,749	$11,920,495

See notes to financial statements.

STATEMENT OF CHANGES IN FINANCIAL POSITION

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973
SOURCE OF FUNDS		
From operations:		
Net earnings for the year	$2,982,254	$2,918,042
Charges (credits) to earnings which did not affect working capital:		
Amortization of excess of carrying amounts of net assets of subsidiary over acquisition cost	(131,130)	(131,130)
Amortization of long-term financing costs	28,202	28,202
Excess of equity in earnings of subsidiary over dividends received	(2,637,388)	(2,510,755)
Equity in earnings of affiliated company	(349,824)	(327,366)
Deferred income taxes (applicable to equity in earnings of affiliated company)	23,990	23,261
TOTAL FROM OPERATIONS	(83,896)	254
Proceeds from long-term borrowing		51,341
Dividend from subsidiary	6,600,000	
	6,516,104	51,595
APPLICATION OF FUNDS		
Loan to subsidiary	6,600,000	
Investment in affiliated company		57,214
	6,600,000	57,214
DECREASE IN WORKING CAPITAL	($ 83,896)	($ 5,619)

	1974	1973
INCREASE (DECREASE) IN COMPONENTS OF WORKING CAPITAL		
Current assets:		
Cash	($ 8,688)	($ 848)
Due from subsidiary	(21,000)	
	(29,688)	(848)
Current liabilities:		
Accrued interest and other expenses	8,093	
Due to subsidiary	46,115	4,771
	54,208	4,771
NET CHANGE	($83,896)	($5,619)

( ) indicate red figure.

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

DIVERSIFIED RETAILING COMPANY, INC.

February 2, 1974 and February 3, 1973

Note A - SIGNIFICANT ACCOUNTING POLICIES

Investment in Subsidiary

The investment in the Company's wholly-owned subsidiary, Associated Retail Stores, Inc. (Associated) (Note B), is accounted for under the equity method. At the date of acquisition of said subsidiary, the carrying amount of the net assets of the subsidiary was in excess of the investment of Diversified in the amount of $1,311,309; this excess is being amortized over a ten-year period and is shown in the balance sheet net of accumulated amortization.

Investment in Affiliated Companies

In compliance with Accounting Principles Board Opinion No. 18 the Company adopted in fiscal 1973 the equity method of accounting for investments in companies in which it has the ability to exercise significant influence through its direct and indirect holdings (Note C). Under this method, which has been applied retroactively, the Company currently recognizes its equity in the net earnings of such affiliates. In determining the amounts reported as equity in earnings of affiliated companies provision has been made for the amortization over a forty-year period of the difference between the cost of the Company's investment and the underlying equity in net assets at the dates of acquisition of the various blocks of stock of the affiliated companies. Deferred income taxes have also been provided on the portion of such equity represented by undistributed earnings. In making this computation it has been assumed that the earnings ultimately would be distributed as dividends and dividends received deductions would be available to offset 85% of the gross dividend.

Financing Costs

Certain costs incurred in connection with the issuance of 8% debentures have been capitalized and are being amortized ratably over the stipulated life of the debentures.

Federal Income Taxes

The Company's policy of filing a consolidated federal income tax return with Associated and Associated's wholly-owned insurance subsidiary, Columbia Insurance Company (formerly Reinsurance Corp. of Nebraska), has resulted in tax credits to Diversified. The investment tax credit (not material) is accounted for as a reduction of federal income taxes in the year in which the credit arises (flow-through method).

NOTES TO FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

February 2, 1974 and February 3, 1973

Note B - INVESTMENT IN SUBSIDIARY

Associated holds common stock of certain affiliated companies (Note C). These investments, as well as Associated's investment in Columbia, are accounted for under the equity method in Associated's statement of earnings, which is summarized below:

	Fiscal year ended February 2, 1974	Fiscal year ended February 3, 1973
Earnings before equity in earnings of unconsolidated subsidiary and affiliated companies	$ 463,616	$ 823,047
Equity in earnings of unconsolidated subsidiary	912,811	954,844
Equity in earnings of affiliated companies	865,383	869,343
Extraordinary gain	395,578	193,021
NET EARNINGS	$2,637,388	$2,840,255

Associated's balance sheet at February 2, 1974 included an $8,429,000 investment in unconsolidated subsidiary (Columbia) and an $11,990,000 investment in affiliated companies (Note C) in the $28,673,000 total assets. Comparable figures for February 3, 1973 were $7,516,000 and $9,552,000 of total assets of $26,705,000. Associated's investment in affiliated companies included $2,267,000 representing the excess of the cost over the underlying equity in net assets at the dates of acquisition of the various blocks of stock.

Note C - INVESTMENT IN AFFILIATED COMPANIES

At February 2, 1974 the Company, Associated and Columbia hold in the aggregate 16% and 11% of the outstanding common stock of Blue Chip Stamps and Berkshire Hathaway Inc., respectively. In addition certain related persons own 32% and 36%, respectively, of the outstanding common stock of these companies. Disposition of all or any lesser amount of said common stock of these affiliated companies may be subject to certain restrictions. Trading in Berkshire common stock is not extensive, although trades have been executed between $70 and $80 per share. A representative fair market value of $75 would cause the holdings of the Company to approximate $1,979,000, exceeding cost. The Company believes that while such market valuations may be indicative of the value in the public market for a moderate number of shares, they are not necessarily indicative of the fair market value of the substantial block of shares held in Berkshire.

The underlying equity in net assets at the dates of the Company's acquisition of the several blocks of Berkshire stock exceeded the Company's cost by $148,118. Berkshire has paid no dividends during the period of the Company's affiliation.

Note C - (Cont'd) The latest Annual Reports for Blue Chip Stamps and Berkshire Hathaway Inc. are included with this filing as Exhibits B and C, respectively, and should be read in conjunction with the financial statements.

Note D - DEBT

Interest and financing costs reflected in the consolidated statements of earnings relate principally to long-term debt.

8% Debentures

The debentures were issued under a trust indenture dated November 1, 1967, under which the aggregate principal amount which may be issued is unlimited, the debentures are not secured by any lien, and there are no restrictions against secured or unsecured borrowings of the Company. They bear interest at a fixed annual rate of 8% payable semi-annually and bear participating additional interest each year up to a maximum of 1% contingent upon the amount of adjusted consolidated earnings before income taxes, as defined, for the previous fiscal year. No contingent interest was payable under these provisions during the last two fiscal years.

The debentures are subject to redemption at the option of the Company at 105% of par plus accrued interest to October 31, 1974 and thereafter at percentages reducing to 100% at November 1, 1983. The debentures are also contingently subject to redemption at par plus accrued interest through operation of a sinking fund. If the adjusted consolidated net worth, as defined, of the Company is less than $12 million, sinking fund payments are generally required. No such contingent sinking fund payments have been required and none appear imminent.

The debentures are further subject to redemption at the option of each debenture holder, exercisable within 60 days following notice that, other than by reason of the death of Warren E. Buffett, said Warren E. Buffett or an organization controlled by him, shall cease to own in combined holdings a larger block of shares with voting rights of the Company than any other stockholder, or combination of stockholders, controlled by a single individual.

The Articles of Incorporation of the Company provide that if and as long as an Event of Default exists or the Adjusted Consolidated Net Worth of the Company is less than $8,000,000, and either condition continues for a period of thirty days, then the holders of the Debentures, to the exclusion of the holders of the Company's stock, shall be entitled to vote (i) to elect directors of the Company, and (ii) to approve the sale, lease or other disposition of all or substantially all of the assets of the Company and distribution of the proceeds thereof to the extent necessary to pay all sums due Debenture holders and other creditors. No amendment to such provisions shall be made as long as any Debentures are outstanding without the written approval of the holders of two-thirds in principal amount of the Debentures then outstanding. If there are such voting rights, each holder of the Debentures will have one vote for each $1,000 principal amount of Debentures.

DIVERSIFIED RETAILING COMPANY, INC.

February 2, 1974 and February 3, 1973

Note D - (Cont'd) The Trust Indenture covering the Debentures contains certain restrictions applicable to the Company relating to net worth, redemption of stock and payment of dividends. Retained earnings of approximately $640,000 were subject to such restrictions at February 2, 1974.

9% Notes Payable

The Notes Payable represent purchase obligations for shares of Berkshire Hathaway Inc. acquired at various dates. These notes become due at varying dates from May 1, 1974 to January 4, 1988 and bear interest at 9% per year, payable semi-annually. The notes are also due on the respective payees' demand on or after the expiration of twelve months following the date of death of Warren E. Buffett.

Principal payments due on these notes are summarized by fiscal year as follows:

1975-76	$ 3,731
1977	109,731
1978-81	3,731
1982	357,969
1983	571,299
1986-87	26,500
1988	128,500

The principal amount maturing within one year has not been separately classified as a current liability.

Note E - INCOME TAXES

The Company's consolidated federal income tax returns have been examined by the Internal Revenue Service through February 1, 1969. In management's opinion, there will be no material assessments for subsequent years.

Note F - STOCKHOLDERS' EQUITY

There were no changes in the capital stock and additional paid-in capital accounts during the fiscal years ended February 2, 1974 and February 3, 1973.

At February 3, 1973 earnings retained in the business included $2,648,000 representing undistributed earnings of subsidiary and affiliated company as follows: Associated - $1,837,000 and Berkshire Hathaway - $811,000.

Note G - PROPOSED MERGER

The Board of Directors of the Company has approved for submission to the shareholders a proposal to merge the Company into Berkshire Hathaway Inc., an affiliate (see Notes A and C). Consummation of the merger is subject to a number of conditions, including the approval of certain regulatory authorities and a favorable stockholders' vote on the part of each corporation. Shares of Berkshire Hathaway Inc. are proposed to be issued to the Company's stockholders in exchange for their holdings in the Company in this transaction.

SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

COL. A	COL. B		COL. C		COL. D		COL. E		COL. F
	BALANCE AT BEGINNING OF PERIOD		ADDITIONS		DEDUCTIONS		BALANCE AT END OF PERIOD		
NAME OF ISSUER AND DESCRIPTION OF INVESTMENT	(1) Number of Shares or Units, Principal Amount of Bonds and Notes	(2) Amount in Dollars	(1) Equity Taken Up in Earnings (Losses) of Affiliates and Other persons for the Period	(2) Other	(1) Distribution of Earnings By Persons in Which Earnings (Losses) Were Taken Up	(2) Other	(1) Number of Shares or Units, Principal Amount of Bonds and Notes	(2) Amount in Dollars	Dividends Received During the Period from Investments Not Accounted for by the Equity Method
Year ended February 2, 1974:									
Unconsolidated subsidiary:									
Columbia Insurance Company									
Common Stock	5,000	$ 7,516,244	$ 912,811				5,000	$ 8,429,055	
Affiliates:									
Blue Chip Stamps									
Common Stock	591,900	$ 8,335,047	$ 627,564		$142,056		591,900	$ 8,820,555	
Berkshire Hathaway Inc.									
Common Stock	41,745	2,924,157	677,768	$1,625,099(5)			60,836	5,227,024	
		$11,259,204	$1,305,332	$1,625,099	$142,056			$14,047,579	

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SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

COL. A	COL. B		COL. C		COL. D		COL. E		COL. F
NAME OF ISSUER AND DESCRIPTION OF INVESTMENT	BALANCE AT BEGINNING OF PERIOD		ADDITIONS		DEDUCTIONS		BALANCE AT END OF PERIOD		Dividends Received During the Period from Investments Not Accounted for by the Equity Method
	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	(1) Equity Taken Up in Earnings (Losses) of Affiliates and Other persons for the Period	(2) Other	(1) Distribution of Earnings By Persons in Which Earnings (Losses) Were Taken Up	(2) Other	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	
Year ended February 3, 1973:									
Unconsolidated subsidiary:									
Columbia Insurance Company									
Common Stock	5,000	$6,561,400	$ 954,844				5,000	$ 7,516,244	
Affiliates:									
Blue Chip Stamps									
Common Stock	291,900	$3,861,318	$ 777,578	$3,838,207(2)	$142,056		591,900	$ 8,335,047	
Berkshire Hathaway Inc.									
Common Stock	29,064	1,491,560	489,498	943,099(3)			41,745	2,924,157	
		$5,352,878	$1,267,076(1)	$4,781,306	$142,056			$11,259,204	

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SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

(PARENT COMPANY ONLY)

COL. A	COL. B		COL. C		COL. D		COL. E		COL. F
	BALANCE AT BEGINNING OF PERIOD		ADDITIONS		DEDUCTIONS		BALANCE AT END OF PERIOD		
NAME OF ISSUER AND DESCRIPTION OF INVESTMENT	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	(1) Equity Taken Up in Earnings (Losses) of Affiliates and Other persons for the Period	(2) Other	(1) Distribution of Earnings By Persons in Which Earnings (Losses) Were Taken Up	(2) Other	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	Dividends Received During the Period from Investments Not Accounted for by the Equity Method
Year ended February 2, 1974:									
Associated Retail Stores, Inc.	453,000	$24,357,260	$2,637,388		$6,600,000		453,000	$20,394,648	
Affiliate:									
Berkshire Hathaway Inc. Common Stock	26,392	$ 1,707,532	$ 349,824(1)				26,392	$ 2,057,356	

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SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

(PARENT COMPANY ONLY)

COL. A	COL. B		COL. C		COL. D		COL. E		COL. F
	BALANCE AT BEGINNING OF PERIOD		ADDITIONS		DEDUCTIONS		BALANCE AT END OF PERIOD		
NAME OF ISSUER AND DESCRIPTION OF INVESTMENT	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	(1) Equity Taken Up in Earnings (Losses) of Affiliates and Other persons for the Period	(2) Other	(1) Distribution of Earnings By Persons in Which Earnings (Losses) Were Taken Up	(2) Other	(1) Number of Shares or Units. Principal Amount of Bonds and Notes	(2) Amount in Dollars	Dividends Received During the Period from Investments Not Accounted for by the Equity Method
Year ended February 3, 1973:									
Associated Retail Stores, Inc.									
Common Stock	453,000	$21,846,505	$2,840,255		$329,500		453,000	$24,357,260	
Affiliate:									
Berkshire Hathaway Inc.									
Common Stock	25,624	$ 1,322,952	$ 327,366(1)	$57,214(4)			26,392	$ 1,707,532	

(1) Reconciliation to statement of operations:

	Consolidated		Parent Company	
Equity in earnings	$1,305,332	$1,267,076	$349,824	$327,366
Applicable income taxes	114,115	93,628	23,990	23,261
	$1,191,217	$1,173,448	$325,834	$304,105

(2) Fair value of 300,000 shares of Blue Chip Stamps, Inc. common stock received in exchange for 270,584 shares of Thriftimart, Inc. common stock (cost $3,562,482) included in other security investments.

(3) Acquisition of 12,681 shares at cost.

(4) Acquisition of 768 shares at cost.

(5) Acquisition of 19,091 shares at cost.

The notes to the consolidated financial statements are made a part hereof.

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SCHEDULE V—PROPERTY, PLANT, AND EQUIPMENT

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

COL. A	COL. B	COL. C	COL. D	COL. E	COL. F
CLASSIFICATION	Balance at Beginning of Period	Additions at Cost	Retirements or Sales	Other Changes—Debit and/or Credit*—Describe (A)	Balance at Close of Period
Fiscal year ended February 2, 1974:					
Land	$ 894,722	$ 19,222	$ 712,429(B)		$ 201,515
Buildings	599,373	57,665	446,841(B)		210,197
Building improvements	154,880	1,215			156,095
Leasehold improvements	351,805	25,202		($ 24,094)	352,913
Furniture, fixtures and equipment	747,412	88,820	17,061	(172,772)	646,399
	$2,748,192	$192,124	$1,176,331	($196,866)	$1,567,119
Fiscal year ended February 3, 1973:					
Land	$ 894,722				$ 894,722
Buildings	599,373				599,373
Building improvements	534,310	$ 3,468		($382,898)	154,880
Leasehold improvements	397,641	11,256	$ 630	(56,462)	351,805
Furniture, fixtures and equipment	791,459	34,222	7,718	(70,551)	747,412
	$3,217,505	$48,946	$8,348	($509,911)	$2,748,192

(A) Represents fully-depreciated assets written off against accumulated depreciation.

(B) Represents cost of property condemned during the year.

The notes to the consolidated financial statements are made a part hereof.

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SCHEDULE VI—ACCUMULATED DEPRECIATION, DEPLETION AND AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

COL. A	COL. B	COL. C	COL. D	COL. E	COL. F
DESCRIPTION	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Retirements	Other Changes—Add (Deduct)—Describe	Balance at End of Period
				(A)	
Fiscal year ended February 2, 1974:					
Buildings	$321,608	$ 9,187	$284,944(B)		$ 45,851
Building improvements	26,460	8,753			35,213
Leasehold improvements	205,026	44,155		($ 24,094)	225,087
Furniture, fixtures and equipment	438,758	83,436	10,048	(172,772)	339,374
	$991,852	$145,531	$294,992	($196,866)	$645,525
Fiscal year ended February 3, 1973:					
Buildings	$ 306,165	$ 15,443			$321,608
Building improvements	397,446	11,912		($382,898)	26,460
Leasehold improvements	204,508	57,309	$ 329	(56,462)	205,026
Furniture, fixtures and equipment	423,693	91,808	6,192	(70,551)	438,758
	$1,331,812	$176,472	$6,521	($509,911)	$991,852

(A) Represents fully-depreciated assets written off against accumulated depreciation.

(B) Represents accumulated depreciation on property condemned during the year.

The notes to the consolidated financial statements are made a part hereof.

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SCHEDULE XVI—SUPPLEMENTARY INCOME STATEMENT INFORMATION

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARY

COL. A	COL. B
ITEM	Charged to Costs and Expenses
Fiscal year ended February 2, 1974:	
Maintenance and repairs	$ 462,130
Depreciation and amortization of property, plant and equipment	145,531
Amortization of intangible assets	28,202
Taxes, other than income taxes:	
Payroll taxes	479,545
Personal property and real estate	179,483
Other	201,434
Rents:	
Real estate	1,843,817
Equipment	67,254
Royalties	None
Advertising	102,414
Research and development	None
Fiscal year ended February 3, 1973:	
Maintenance and repairs	421,521
Depreciation and amortization of property, plant and equipment	176,472
Amortization of intangible assets	28,202
Taxes, other than income taxes:	
Payroll taxes	410,531
Personal property and real estate	203,622
Other	121,736
Rents:	
Real estate	1,771,966
Equipment	64,866
Royalties	None
Advertising	97,425
Research and development	None

COLUMBIA INSURANCE COMPANY

Financial Information for Inclusion in Annual 10-K Report

December 31, 1972 and 1973

PEAT, MARWICK, MITCHELL & CO.

CERTIFIED PUBLIC ACCOUNTANTS

ACCOUNTANTS' REPORT

The Board of Directors
Columbia Insurance Company:

We have examined the financial statements and related schedules of Columbia Insurance Company as listed in the accompanying index. 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. We did not examine the financial statements of Blue Chip Stamps, a significant nonconsolidated affiliated company, which statements were examined by other auditors whose qualified report thereon has been furnished to us. Our opinion expressed herein, insofar as it relates to Blue Chip Stamps included in stock of affiliates, $3,498,635 and $3,670,302 at December 31, 1972 and 1973, respectively, and $294,779 and $203,767 in equity in net earnings of other companies for 1972 and 1973, respectively, is based solely upon the report of the other auditors.

We have reviewed the audited financial statements issued by Blue Chip Stamps for the year ended March 2, 1974 and noted the pending legal proceedings, resulting in a qualified opinion on such financial statements by the other auditors. These legal proceedings are explained in note 5 to the financial statements.

In our opinion, based upon our examination and the report of the other auditors and subject to the effect, if any, upon the investment in Blue Chip Stamps resulting from the ultimate outcome of the legal proceedings referred to in the preceding paragraph, the aforementioned financial statements present fairly the financial position of Columbia Insurance Company at December 31, 1972 and 1973 and the results of its operations and changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis; and the supporting schedules, as listed in the accompanying index, in our opinion, present fairly the information set forth therein.

PEAT, MARWICK, MITCHELL & CO.

Omaha, Nebraska
March 18, 1974

COLUMBIA INSURANCE COMPANY

Index to Financial Statements

Schedules III, IV, VIII and IX are omitted because they are not applicable.

COLUMBIA INSURANCE COMPANY

Balance Sheets

December 31, 1972 and 1973

Assets	1972	1973
Bonds, at amortized value	$ 1,058,203	1,701,560
Common stocks:		
Other than stocks of affiliates	1,187,548	1,391,572
Berkshire Hathaway Inc. (note 2)	3,535,442	4,178,367
Blue Chip Stamps (note 3)	3,498,635	3,670,302
	8,221,625	9,240,241
Cash and bank deposits	16,266	13,608
Uncollected premiums (net of commissions payable of $81,205, 1972; $89,872, 1973)	272,738	389,289
Investment income due and accrued	46,406	29,905
Prepaid acquisition costs	143,000	142,000
Other assets	345	186
	$ 9,758,583	11,516,789

Liabilities, Capital Stock and Surplus	1972	1973
Losses and claims	$ 1,005,227	1,493,040
Loss adjustment expenses	171,485	167,471
Unearned premiums	845,259	902,893
Assumed losses payable	64,738	260,611
Federal income taxes (note 6):		
Current	794	29,522
Deferred	153,258	223,882
	154,052	253,404
Other liabilities	1,578	10,315
	2,242,339	3,087,734
Capital stock and surplus:		
Capital stock par value $100. Authorized, issued and outstanding, December 31, 1972 - 5,000 shares; December 31, 1973 - 20,000 shares (note 4)	500,000	2,000,000
Surplus:		
Paid-in	5,355,389	3,855,389
Unassigned	1,660,855	2,573,666
Total surplus	7,016,244	6,429,055
Total capital stock and surplus	7,516,244	8,429,055
	$ 9,758,583	11,516,789

See accompanying notes to financial statements.

COLUMBIA INSURANCE COMPANY

Statements of Earnings

Years ended December 31, 1972 and 1973

	1972	1973
Underwriting income:		
Net premiums written	$ 1,834,106	2,161,947
Increase in unearned premiums	124,870	57,634
Premiums earned	1,709,236	2,104,313
Losses incurred	1,159,875	1,367,098
Loss expense incurred	128,568	89,164
	1,288,443	1,456,262
	420,793	648,051
Underwriting expenses incurred:		
Commissions and brokerage	347,294	528,148
Taxes, licenses and fees	3,788	31,124
Other underwriting expenses	4,508	20,036
Decrease in prepaid acquisition costs	21,320	1,000
	376,910	580,308
Gain from underwriting	43,883	67,743
Investment income:		
Interest on bonds	75,661	99,083
Dividends, unaffiliated companies	74,148	58,078
	149,809	157,161
Investment expenses	1,226	1,840
Net investment income	148,583	155,321
Earnings before Federal income taxes, equity in net earnings of other companies and realized investment gain (loss)	192,466	223,064
Federal income taxes (note 6):		
Current	-	48,087
Deferred	38,000	1,000
	38,000	49,087
Earnings before equity in net earnings of other companies and realized investment gain (loss)	154,466	173,977
Equity in net earnings of other companies:		
Berkshire Hathaway Inc. (note 2)	504,013	590,321
Blue Chip Stamps (note 3)	294,779	203,767
	798,792	794,088
Earnings before realized investment gain (loss)	953,258	968,065
Realized investment gain (loss)	2,266	(78,934)
Applicable Federal income tax (benefit)	680	(23,680)
Net realized investment gain (loss)	1,586	(55,254)
Net earnings	$ 954,844	912,811

See accompanying notes to financial statements.

COLUMBIA INSURANCE COMPANY

Statements of Capital Stock and Surplus

Years ended December 31, 1972 and 1973

	Capital stock	Surplus Paid-in	Surplus Unassigned
Balance, December 31, 1971	$ 500,000	5,355,389	706,011
Net earnings for the year	-	-	954,844
Balance, December 31, 1972	500,000	5,355,389	1,660,855
Net earnings for the year	-	-	912,811
Transfer to capital stock representing par value of shares issued as a result of four-for-one stock split	1,500,000	(1,500,000)	-
Balance, December 31, 1973	$ 2,000,000	3,855,389	2,573,666

See accompanying notes to financial statements.

COLUMBIA INSURANCE COMPANY

Statements of Changes in Financial Position

Years ended December 31, 1972 and 1973

		1972	1973
Funds provided:			
From operations:			
Net earnings	$	954,844	912,811
Charges (credits) to earnings not requiring (providing) funds:			
Amortization of bond discount		(5,346)	(5,324)
Increase in estimated losses and loss expenses		680,674	483,799
Increase in unearned premiums		124,870	57,634
Increase in assumed losses payable		4,372	195,873
Increase in deferred taxes		38,000	1,000
Increase (decrease) in accrued taxes and expenses		(84,641)	37,465
Decrease (increase) in uncollected premiums		56,692	(116,551)
Decrease (increase) in accrued investment income		(22,977)	16,501
Decrease in prepaid acquisition costs		21,320	1,000
Loss on sale of investments		-	78,934
Equity in undistributed earnings of affiliated companies, net of deferred taxes		(738,792)	(738,408)
Amortization of organization expense		160	159
Funds provided from operations		1,029,176	924,893
From investments sold or matured:			
Bonds		750,814	98,716
Common stocks, other than stocks of affiliates		21,834	676,816
		772,648	775,532
Decrease in cash		-	2,658
Total funds provided	$	1,801,824	1,703,083
Funds used:			
Cost of investments purchased:			
Bonds		762,059	736,749
Common stocks:			
Other than stocks of affiliates		5,562	959,774
Affiliates		1,031,965	6,560
		1,037,527	966,334
		1,799,586	1,703,083
Increase in cash		2,238	-
Total funds used	$	1,801,824	1,703,083

See accompanying notes to financial statements.

COLUMBIA INSURANCE COMPANY

Notes to Financial Statements

December 31, 1972 and 1973

(1) Summary of Significant Accounting Policies and Practices

(a) Insurance Premiums

Insurance premiums are recognized as revenues ratably over the terms of the policies. Unearned premiums are computed on the monthly pro rata basis. Policy acquisition costs or commissions are deferred and charged against income ratably over the terms of the policies.

(b) Securities

Investments in bonds are stated at cost, adjusted where appropriate for amortization of premium or accretion of discount. Investments in common stocks other than affiliates are stated at cost. Certain bonds and stocks deposited in trust with regulatory authorities or with ceding reinsurers in accordance with various reinsurance treaties were as follows:

	1972	1973
Bonds at amortized cost	$ 295,238	895,769
Stocks	1,369,682	1,522,682
	$ 1,664,920	2,418,451

(c) Estimated Losses

The provision for losses and loss adjustment expenses is based upon past experience and estimates received relating to assumed reinsurance and estimates of unreported losses.

(d) Catastrophe Losses

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

(e) Income Taxes

The Company accounts for certain income and expense items differently for financial reporting purposes than for income tax purposes. Provisions for deferred taxes are being made in recognition of these timing differences.

The Company, a 100% owned subsidiary of Associated Retail Stores, Inc. (ARS), joins ARS and its parent in filing a consolidated Federal income tax return. It is the policy of the Company to accrue appropriate income taxes on the unremitted earnings of affiliates.

(f) Investments in Affiliated Companies

The Company holds common stock investments in Berkshire Hathaway Inc., and Blue Chip Stamps which two companies are considered "investees" under the provisions of Accounting Principles Board Opinion No. 18. Accordingly, the Company uses the equity method of accounting for these investments, under which method the Company currently recognizes its proportionate share of earnings reported by those companies, net of deferred income taxes provided for under the assumption that such earnings will ultimately be distributed as taxable dividends. Provision is also made for amortization of the difference between cost of the investments and the underlying equity in net assets at the dates of acquisition; this provision through the year ended December 31, 1972 was computed on the basis of a forty year amortization period. With respect to the investment in Blue Chip Stamps, effective for the year ended December 31, 1973, the period of amortization of excess cost was reduced to seven remaining years from the beginning of the current fiscal year. This change has the effect of reducing income for the year ended December 31, 1973 by $126,000. In the

(Continued)

opinion of management, this change was necessary because of the anticipated continuing decline in the stamp operation of Blue Chip Stamps to which the excess cost originally related.

Blue Chip Stamps determines income on the basis of a fiscal year ending on or about February 28; the Company has not recognized this difference in its annual accounting for its equity in earnings of Blue Chip, having recorded its equity in earnings of Blue Chip's year ending with respect to February 28 in its year ending with respect to the preceding December 31.

(2) Investment in Berkshire Hathaway Inc.

The carrying value of the investment in common stock of Berkshire Hathaway Inc. represents the cost plus the equity in earnings since dates of acquisition, adjusted for amortization on a forty year basis, of the excess cost over underlying net asset values at dates of acquisition. This is summarized as follows:

	December 31, 1972	December 31, 1973
Shares owned	48,635	48,715
Percentage of total outstanding shares (approximate)	5%	5%
Cost represented by:		
Underlying net asset values at dates of acquisition	$ 2,663,148	2,668,740
Excess cost, net of amortization of $1,072 at December 31, 1972 and $4,241 at December 31, 1973	125,731	123,528
	2,788,879	2,792,268
Equity in post-acquisition earnings	746,563	1,386,099
Carrying value	$ 3,535,442	4,178,367

Deferred income taxes of approximately $54,000 at December 31, 1972 and $100,000 at December 31, 1973 have been provided with respect to the equity in post-acquisition earnings, assuming their ultimate distribution as a taxable dividend.

(3) Investment in Blue Chip Stamps

The carrying value of the investment in 250,000 shares of common stock of Blue Chip Stamps (approximately 5% of the total outstanding shares) represents the cost plus the equity in undistributed earnings since dates of acquisition, adjusted for amortization of the excess cost over underlying net asset values at dates of acquisition. This is summarized as follows:

	December 31, 1972	December 31, 1973
Cost represented by:		
Underlying net asset values at dates of acquisition	$ 1,912,829	1,912,829
Excess cost, net of amortization of $39,812 at December 31, 1972 and $195,645 at December 31, 1973	1,148,234	992,401
	3,061,063	2,905,230
Equity in post-acquisition undistributed earnings	437,572	765,072
Carrying value	$ 3,498,635	3,670,302

Through December 31, 1972, the excess cost over underlying net asset values was being written off over a forty-year period. Commencing with the current fiscal year, this period of amortization was reduced to seven years (see note 1).

(Continued)

Deferred income taxes of approximately $31,500 at December 31, 1972 and $55,000 at December 31, 1973 have been provided with respect to the equity in post-acquisition undistributed earnings, assuming their ultimate distribution as a taxable dividend.

(4) Stock Split

On April 26, 1973, the Board of Directors declared a four-for-one stock split. In connection therewith, $1,500,000, representing the par value of the additionally issued shares, was transferred from paid-in surplus to capital stock.

(5) Legal Proceedings of Blue Chip Stamps

The financial statements of Blue Chip Stamps include the following note (The "Company" refers to Blue Chip Stamps):

"Pursuant to a consent final judgment entered in 1967, the Company in June 1972 submitted for approval by the United States District Court a plan to offer for sale one third of its California trading stamp business located within a contiguous geographical area in Southern California. In January 1973, the Court made an order (1) disapproving said plan, (2) requiring the Company to continue efforts to negotiate a sale and (3) calling for the appointment of an independent expert to study the feasibility of a sale or spin-off of a portion of the Company's trading stamp business under existing conditions. The report of the independent expert has not yet been filed with the Court. The Company believes that such a sale or spin-off, if consummated under existing market conditions, would compel the Company to discontinue issuance of its trading stamps.

The Company is a defendant in a purported class action filed March 1, 1971 to recover for stamp savers monies collected by it as reimbursement for California sales taxes on redemption of stamps. Plaintiffs claim that redemption transactions are not taxable and that all such collections should be returned, or alternatively, that such collections exceeded the tax properly payable and such excess should be returned. The Company has paid sales taxes to the state equal to its reimbursement collections. The Company has asserted claims against the state for reimbursement of all or part of any recovery by plaintiffs. Following denial of these claims by the state, the Company cross-complained against the state seeking indemnity. The original complaint was amended to assert fraud and to seek punitive damages. On June 1, 1973 two partial summary judgments were entered by way of interlocutory orders, neither of which has yet become final or appealable. The first was in favor of the Company to the effect that the redemption transactions were taxable. The second was in favor of plaintiffs to the effect that the Company's collections exceeded the tax properly payable. In the opinion of counsel for the Company the second partial summary judgment was erroneous. Issues relating to the class action aspects of the case remain unresolved along with a number of issues of fact. Maximum liability in respect of this action is estimated at $7,000,000 less the amount of any money which may be recovered on the claims against the state. Counsel believes the prospects for such recovery to be good. In the opinion of counsel for the Company, substantial defenses are available, but counsel cannot predict the ultimate outcome of the action.

(Continued)

COLUMBIA INSURANCE COMPANY

Notes to Financial Statements, Continued

A purported class action was filed on November 10, 1970 against the Company and certain of its present and former stockholders and directors. The complaint was filed on behalf of retailer users of Blue Chip Stamps who failed to purchase stock of the Company in a 1968 offering to retailer users. The complaint alleges damages to plaintiffs of $21,400,000, together with exemplary damages of $25,000,000, interest, attorneys' fees and costs, and prays that plaintiffs have the right to purchase stock, or units of stock and debentures, of the Company on the terms of the 1968 offering. The action was dismissed with prejudice by the United States District Court. On October 15, 1973 a panel of three judges of the United States Court of Appeals for the Ninth Circuit reversed the prior dismissal by the District Court and remanded the case for further proceedings. In a two-to-one opinion, the panel held that a class of persons who were entitled to but failed to purchase securities of the Company in connection with the 1968 offering had standing to sue for damages under Rule 10b-5 of the Securities Exchange Act of 1934, if they could prove that such failure to purchase was induced by alleged fraudulent representations of the Company and certain of its past and present officers, directors and shareholders. On April 1, 1974 the Ninth Circuit denied a petition for rehearing and a request that the case be heard by the entire panel of judges of the Ninth Circuit. The defendants will seek a review by the United States Supreme Court. On June 21, 1971 plaintiffs filed a substantially identical action against the same defendants in the Los Angeles County Superior Court, but the Company has not yet been served with process in that action. In the opinion of counsel for the Company, upon the facts now known and the present state of the law, there appear to be substantial defenses on the merits to the complaints in both the federal and state actions.

The Company, together with a number of oil companies and supermarket chains, was named as defendant in an antitrust action filed on July 12, 1971 by a California corporation formerly engaged in the trading stamp business. The complaint seeks treble damages in substantial amounts plus attorneys' fees and costs. The Company has not been served with process. In the opinion of counsel for the Company, upon the facts known, the action is without substantial merit."

(6) Federal Income Taxes

Federal income tax expense is made up of the following:

	1972	1973
Current Federal income tax expense (benefit) related to:		
Earnings before Federal income taxes, equity in net earnings of other companies and realized investment gain (loss)	$ -	48,087
Distributed earnings of Blue Chip Stamps	-	4,320
Realized investment gain (loss)	680	(23,680)
Deferred Federal income tax expense (credit) relating to:		
Equity in undistributed earnings of other companies:		
Berkshire Hathaway Inc.	39,209	46,046
Blue Chip Stamps	20,520	23,580
Accreted discount on bonds	4,000	1,500
Provision (credit) for tax effect of increase (reduction) in deferred acquisition costs	34,000	(500)
	$ 98,409	99,353

(Continued)

COLUMBIA INSURANCE COMPANY

Notes to Financial Statements, Continued

Total Federal income tax expense of $98,409 for 1972 and $99,353 for 1973 amounted to effective rates of 9.3% and 9.8% of income before taxes in those respective years. The tax expense is less than that computed by applying the Federal income tax rate of 48% to income before taxes; the reasons for the difference were as follows:

	1972		1973	
	Amount	Rate	Amount	Rate
Tax expense at statutory rate	$ 505,561	48.0%	$ 485,839	48.0%
Increase (reduction) in income taxes resulting from:				
Tax-exempt interest	(30,576)	(2.9)	(30,576)	(3.0)
85% dividends received credit relating to:				
Dividends received from unaffiliated companies	(30,252)	(2.9)	(23,696)	(2.3)
Equity in net earnings of other companies	(362,942)	(34.5)	(419,030)	(41.4)
Amortization of cost in excess of the underlying equity in net assets of affiliated companies	14,901	1.4	76,321	7.5
Other	1,717	.2	10,495	1.0
	$ 98,409	9.3%	$ 99,353	9.8%

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COLUMBIA INSURANCE COMPANY

Bonds

December 31, 1973

Name of issuer and title of issue	Principal amount of bonds and notes	Actual cost	Book value (amortized cost)	Market value	Amortized value	Admitted asset value
U. S. Government -						
U. S. Treasury Bills	$ 675,000	662,589	662,589	662,589	662,589	662,589
Special revenue and special assessment:						
Alabama, Montgomery Industrial Revenue	100,000	100,000	100,000	100,000	100,000	100,000
Arkansas, Danville Industrial Development Revenue	105,000	105,000	105,000	105,000	105,000	105,000
Georgia, Washington-Wilker Payroll Authority	100,000	100,000	100,000	100,000	100,000	100,000
Illinois Toll Road Commission	125,000	91,875	95,996	95,996	95,996	95,996
Indiana Toll Road Commission	150,000	90,000	99,064	99,064	99,064	99,064
Iowa, Burlington Industrial Revenue	100,000	99,000	99,125	99,125	99,125	99,125
Kansas, Lenexa Industrial Revenue	100,000	100,000	100,000	100,000	100,000	100,000
Louisiana, Beauregard Parish Industrial Revenue	20,000	16,100	16,686	16,686	16,686	16,686
Missouri, New Madrid Industrial Revenue	100,000	80,750	83,621	83,621	83,621	83,621
Missouri, Rolla Industrial Revenue	100,000	95,005	96,277	96,277	96,277	96,277
	1,000,000	877,730	895,769	895,769	895,769	895,769
Industrial and miscellaneous -						
F.M.C. Corporation Convertible Subordinated Debentures	200,000	143,180	143,202	130,000	143,202	143,202
	$ 1,875,000	1,683,499	1,701,560	1,688,358	1,701,560	1,701,560

Schedule I

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COLUMBIA INSURANCE COMPANY

Stocks - Other than Stocks of Affiliates

December 31, 1973

Name of issuer and title of issue	Number of shares	Actual cost	Book value (cost)	Market value	Admitted asset value
Public utilities - California Water Service Co.	11,062	$ 275,449	275,449	273,785	273,785
Banks, trusts and insurance companies:					
Cleveland Trust Company	10	802	802	722	722
Girard Company	100	5,025	5,025	4,450	4,450
Harris Bancorp., Chicago	50	2,512	2,512	2,600	2,600
National Detroit Corp.	100	5,112	5,112	3,838	3,838
New England Merchants Co., Inc.	100	2,313	2,313	1,850	1,850
Omaha National Corporation	8,800	118,641	118,641	176,000	176,000
Pittsburgh National Corporation	100	3,513	3,513	3,238	3,238
State Street Boston Financial	50	1,988	1,988	1,800	1,800
Third National Corp., Nashville	200	4,575	4,575	5,500	5,500
	9,510	144,481	144,481	199,998	199,998
Industrial and miscellaneous:					
Boeing Company	100	2,177	2,177	1,238	1,238
Grumann Corporation	100	1,723	1,723	8,375	8,375
Investors Diversified Services, CI. "B"	100	848	848	500	500
Kennecott Copper Corporation	100	2,735	2,735	4,425	4,425
Morse Shoe, Inc.	20,000	153,100	153,100	75,000	75,000
Munsingwear, Inc.	5,000	90,722	90,722	73,125	73,125
Northrup Corporation	100	1,952	1,952	1,738	1,738
Post Corporation	5,200	55,900	55,900	49,400	49,400
Vornado, Inc.	57,600	660,052	660,052	201,600	201,600
Washington Post Company "B"	100	2,433	2,433	1,700	1,700
	88,400	971,642	971,642	417,101	417,101
Total common stocks		$ 1,391,572	1,391,572	890,884	890,884

Schedule II

Note - Market value per NAIC Book of Valuation of Securities.

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COLUMBIA INSURANCE COMPANY

Summary of Investments in Securities - Other than Securities of Affiliates

December 31, 1973

Type of security	Actual cost	Book value	Market value*	Amortized value	Admitted asset value
Bonds and notes:					
U. S. Government	$ 662,589	662,589	662,589	662,589	662,589
Special revenue and special assessment	877,730	895,769	895,769	895,769	895,769
Industrial and miscellaneous	143,180	143,202	130,000	143,202	143,202
Total bonds and notes	1,683,499	1,701,560	1,688,358	1,701,560	1,701,560
Stocks:					
Common stocks:					
Public utilities	275,449	275,449	273,785	-	273,785
Banks, trusts and insurance companies	144,481	144,481	199,998	-	199,998
Industrial and miscellaneous	971,642	971,642	417,101	-	417,101
Total stocks	1,391,572	1,391,572	890,884	-	890,884
Total investments in securities - other than securities of affiliates	$ 3,075,071	3,093,132	2,579,242	1,701,560	2,592,444

*"Market value" is the valuation published in the NAIC Book of Valuation of Securities; in accordance with said book the major portion of the bonds are reflected at amortized cost.

Schedule V

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COLUMBIA INSURANCE COMPANY

Investments in Stocks of Affiliates

December 31, 1973

Name of issuer	Number of shares	Actual cost	Equity in net assets and excess cost	Market value	Admitted asset value
Berkshire Hathaway Inc.	48,715	$ 2,796,511	4,178,367	3,799,770	3,799,770
Blue Chip Stamps	250,000	3,100,875	3,670,302	1,812,500	1,812,500
	298,715	$ 5,897,386	7,848,669	5,612,270	5,612,270

Note - Market value per NAIC Book of Valuation of Securities.

Schedule VI

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COLUMBIA INSURANCE COMPANY

Premiums, Losses and Underwriting Expenses

Year ended December 31, 1972

Line of insurance	Part 1 - Premiums: Unearned premiums beginning of period	Net premiums written	Unearned premiums end of period	Premiums earned during period	Part 2 - Losses and underwriting expenses: Losses incurred during period	Loss expense incurred during period	Commissions and brokerage incurred during period	Other under-writing expense incurred during period
Fire	$ 254,843	349,707	252,858	351,692	208,327			
Allied lines	31,765	107,984	59,907	79,842	42,703			
Homeowners multiple peril	58	344	118	284	-			
Commercial multiple peril	7,158	109,675	42,480	74,353	53,523			
Inland marine	11,641	38,500	16,436	33,705	16,492			
Workmen's compensation	758	26,403	8,526	18,635	2,304			
Liability other than auto	34,163	288,893	87,343	235,713	117,090			
Auto liability	33,829	740,932	249,139	525,622	392,681			
Auto physical damage	340,917	65,896	71,931	334,882	267,164			
Aircraft (all perils)	822	13,871	-	14,693	1,802			
Surety	4,400	9,944	8,417	5,927	6,874			
Burglary and theft	13	246	112	147	-			
Boiler and machinery	22	334	183	173	60			
International	-	48,467	20,286	28,181	21,528			
Reinsurance	-	32,910	27,523	5,387	29,327			
	$ 720,389	1,834,106	845,259	1,709,236	1,159,875	128,568	347,294	8,296

Schedule VII

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COLUMBIA INSURANCE COMPANY

Premiums, Losses and Underwriting Expenses

Year ended December 31, 1973

Line of insurance	Part 1 - Premiums: Unearned premiums beginning of period	Part 1 - Premiums: Net premiums written	Part 1 - Premiums: Unearned premiums end of period	Part 1 - Premiums: Premiums earned during period	Part 2 - Losses and underwriting expenses: Losses incurred during period	Part 2 - Losses and underwriting expenses: Loss expense incurred during period	Part 2 - Losses and underwriting expenses: Commissions and brokerage incurred during period	Part 2 - Losses and underwriting expenses: Other under-writing expense incurred during period
Fire	$ 252,858	386,695	279,125	360,428	450,120			
Allied lines	59,907	56,465	2,590	113,781	(17,098)			
Homeowners multiple peril	118	297	138	277	-			
Commercial multiple peril	42,480	39,795	10,019	72,256	36,031			
Ocean marine	-	3,331	2,037	1,294	620			
Inland marine	16,436	18,188	10,738	23,886	11,830			
Earthquake	-	1,640	-	1,640	(422)			
Workmen's compensation	8,526	29,218	6,117	31,627	14,765			
Liability other than auto	87,343	349,498	166,296	270,545	105,845			
Auto liability	249,139	635,983	143,742	741,381	472,719			
Auto physical damage	71,931	(4,416)	13,131	54,384	35,560			
Aircraft (all perils)	-	4,128	2,200	1,928	4,845			
Surety	8,417	3,125	5,254	6,288	3,118			
Burglary and theft	112	378	224	265	490			
Boiler and machinery	183	241	-	425	57			
International	20,286	44,630	19,865	45,051	24,989			
Reinsurance	27,523	592,751	241,417	378,857	223,629			
	$ 845,259	2,161,947	902,893	2,104,313	1,367,098	89,164	528,148	51,160

Schedule VII

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Schedule X

COLUMBIA INSURANCE COMPANY

Income from Dividends - Equity in Net Profit of Affiliates

Year ended December 31, 1972

Name of issuer and title of issue	Amount of cash dividends	Amount of equity in net profit
Public utilities - California Water Service Co.	$ 19,469	-
Banks, trusts and insurance companies:		
Cleveland Trust Company	26	-
Girard Company	600	-
Harris Trust and Savings of Chicago	100	-
National Bank of Detroit	228	-
New England Merchants Co., Inc.	140	-
Omaha National Corporation	10,912	-
Pittsburgh National Corporation	142	-
State Street Boston Financial	120	-
Third National Bank of Nashville, Tennessee	150	-
	12,418	-
Industrial and miscellaneous:		
Berkshire Hathaway Inc.	-	504,013*
Boeing Company	20	-
Blue Chip Stamps	-	294,779*
Grumann Corporation	25	-
Investors Diversified Services	11	-
Kennecott Copper Corporation	100	-
New Yorker Magazine, Inc.	42,000	-
Northrup Corporation	75	-
Rheingold Corporation	10	-
Washington Post Company	20	-
	42,261	798,792
	$ 74,148	798,792

*Represents equity in net earnings after amortization of excess cost and provision for income taxes.

Schedule X

COLUMBIA INSURANCE COMPANY

Income from Dividends - Equity in Net Profit of Affiliates

Year ended December 31, 1973

Name of issuer and title of issue	Amount of cash dividends	Amount of equity in net profit
Public utilities - California Water Service Co.	$ 21,681	-
Banks, trusts and insurance companies:		
Cleveland Trust Company	46	-
Girard Company	381	-
Harris Bancorp., Chicago	131	-
National Detroit Corp.	236	-
New England Merchants Co., Inc.	175	-
Omaha National Corporation	12,056	-
Pittsburgh National Corporation	189	-
State Street Boston Financial	150	-
Third National Corp., Nashville	250	-
	13,614	-
Industrial and miscellaneous:		
Berkshire Hathaway Inc.	-	590,321*
Boeing Company	40	-
Blue Chip Stamps	-	203,767*
Grumann Corporation	15	-
Investors Diversified Services	45	-
Kennecott Copper Corporation	170	-
Morse Shoe, Inc.	4,750	-
Munsingwear, Inc.	1,350	-
New Yorker Magazine, Inc.	15,000	-
Northrup Corporation	125	-
Post Corporation	1,248	-
Washington Post Company	40	-
	22,783	794,088
	$ 58,078	794,088

*Represents equity in net earnings after amortization of excess cost and provision for income taxes.

Schedule XI

COLUMBIA INSURANCE COMPANY

Summary of Realized Gains (Losses) on Sale or Maturity of Investments

Year ended December 31, 1972

Type of security	Aggregate cost	Aggregate proceeds	Gain (loss)
Stocks:			
Banks, trusts and insurance companies	$ 20,100	21,900	1,800
Industrial and miscellaneous	1,734	2,200	466
	$ 21,834	24,100	2,266
Income taxes applicable to realized gains			680
Net realized gains			$ 1,586

Year ended December 31, 1973

Type of security	Aggregate cost	Aggregate proceeds	Gain (loss)
Stocks:			
Industrial and miscellaneous	$ 755,750	676,816	(78,934)
Income tax benefit applicable to realized losses			23,680
Net realized losses			$(55,254)

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EXHIBIT A

COMPUTATION OF EARNINGS PER SHARE

	Fiscal year ended				
	February 2, 1974	February 3, 1973	January 29, 1972	January 30, 1971	January 31, 1970
Average shares outstanding (1)	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Net earnings	$2,982,254(6)	$2,918,042(4)	$1,515,880(3)(5)	$1,720,265(5)	$ 114,203(2)(5)
Per share amount	$ 2.98	$ 2.92	$ 1.52	$ 1.72	$ .11

(1) Average shares outstanding have been recast to reflect a 3,333-1/3 to 1 stock split which occurred in December 1969.

(2) Includes extraordinary loss of $1,318,979.

(3) Includes extraordinary loss of $111,000.

(4) Includes extraordinary gain of $193,021.

(5) Restated to reflect change in 1973 to equity method of accounting for investments in affiliated companies.

(6) Includes extraordinary gain of $395,578.

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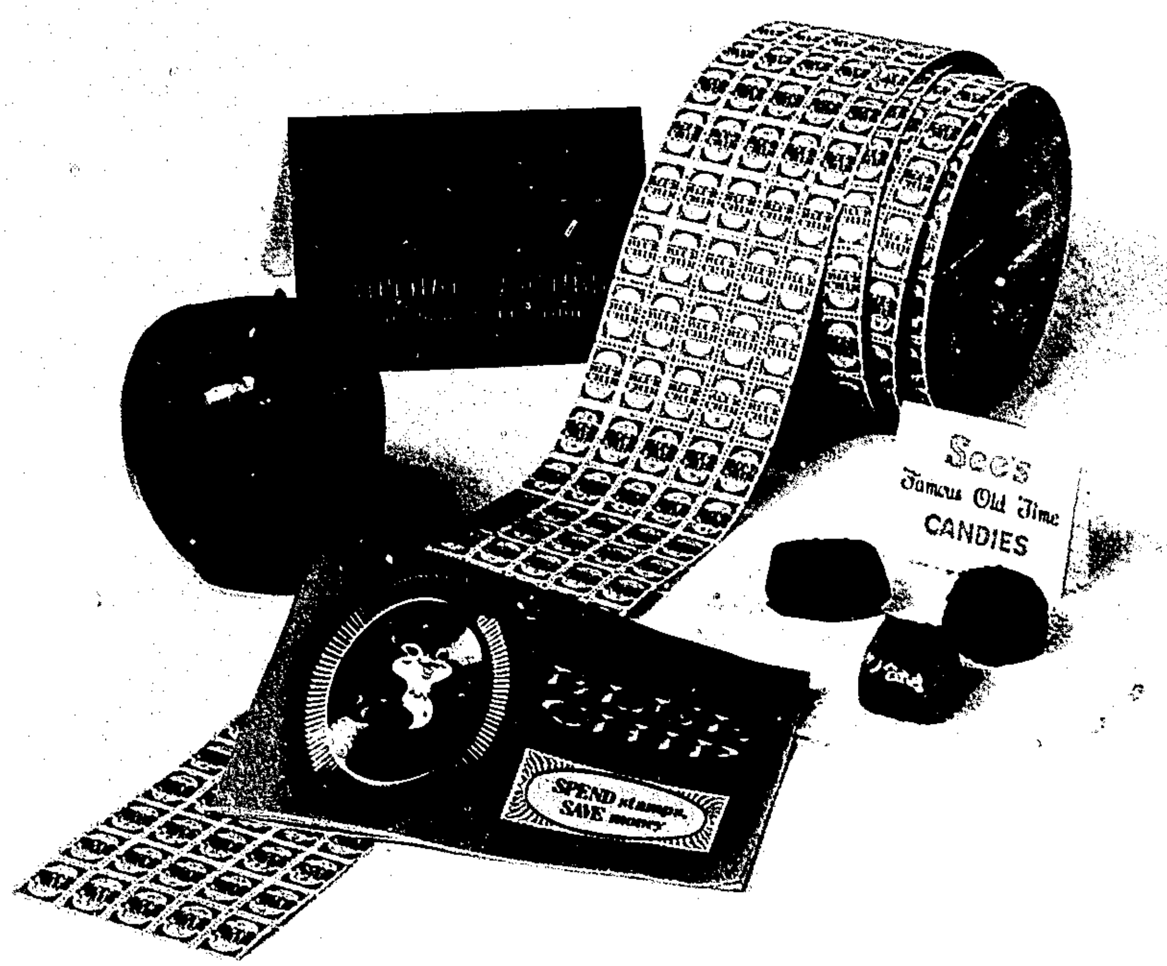
Blue Chip Stamps 1974 Annual Report



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Financial Highlights

Fifty-two Weeks Ended March 2, 1974 and March 3, 1973

	1974	1973
Total revenues	$102,219,000	$132,323,000
Stamp service revenues	51,375,000	88,736,000
Incentive sales	6,261,000	3,624,000
Candy sales	35,780,000	32,049,000
Income before securities losses and extraordinary charges	8,190,000	8,108,000
Securities losses	(185,000)	(82,000)
Extraordinary charges	–	(925,000)
Net income	8,005,000	7,101,000
Per share		
Income before securities losses and extraordinary charges	$ 1.58	$ 1.58
Net income	1.55	1.38
Book value	11.56	10.26

The cover photo depicts Blue Chip Stamps' trading stamp business and its diversification into other operations. The apple is the insignia of Blue Chip Incentives, emblematic of the motivational programs it designs for businesses. Quality candy has made fifty-year old See's Candy Shops, Incorporated famous throughout the West. Mutual Savings and Loan Association of Pasadena is the operating subsidiary of Wesco Financial Corporation, Blue Chip's latest acquisition.

To Our Stockholders

Eighteen years ago Blue Chip Stamp Company, our predecessor, came into being. As its first employee, and a temporary one at that, I cannot help but marvel at the metamorphosis Blue Chip has undergone and is still undergoing.

Prior to the reorganization in 1968, when Blue Chip Stamp Company was merged into Blue Chip Stamps and stock was first offered to the public, we confined our efforts to the issuance and redemption of trading stamps. Our marketable securities consisted mainly of municipal bonds.

Since then we have acquired See's Candy Shops, Inc. and 57% of Wesco Financial Corporation, a high quality savings and loan holding company. Our Incentive Division is growing at an accelerating pace. Our marketable securities have been completely restructured to reflect our long-term objective of maximizing after-tax yield and sound value.

Trading stamps generally—and Blue Chip stamps are no exception—have taken a "licking" due to the advent of a new type of supermarket promotion loosely described as "discounting." When a grocery company "goes discount," it typically reduces the variety of sizes and brands, shortens operating hours and stops issuing trading stamps. It then uses the promotion dollars to advertise its discount policy. I agree with Mr. William S. Beinecke, Chairman of the Sperry and Hutchinson Company, who recently said, "Beyond 1974 and with the moderation of inflation, we see opportunities for recovery in food retailing...because of developing consumer discontent with the claims of 'discounting'." To this I might add: traditionally, when all of the supermarkets are pursuing the same promotion policy, one of them eventually decides it wants to be different from the rest and goes off in another direction, thus starting a new trend.

The shortage of gasoline has virtually eliminated promotional activities at the service station level. It is difficult to predict when supplies of gasoline will be sufficient to rekindle brand competition, but it is clear that far fewer but larger retail outlets will be dispensing gasoline in the future, and at some point in time they will again use point-of-purchase promotions, including trading stamps, to attract and hold customers.

These factors have had an impact on our revenues and earnings. Stamp service revenues were down from $88,736,000 last fiscal year to $51,375,000 for the current fiscal year. More significantly, stamp service revenues declined from $21,159,000 in last year's fourth quarter to $8,774,000 in this year's fourth quarter. Total revenues suffered much less in each case due to increased revenues from our other activities. Income before securities losses, which benefited substantially this year from inclusion of our share of Wesco's net income, held even at $1.58 per share for the year, but dropped from $.70 in last year's fourth quarter to $.62 in this year's fourth quarter. It should be noted that the near-term profit trend for the savings and loan industry appears less favorable.

At our May annual meeting we will ask our stockholders to approve a change in our corporate name from *Blue Chip Stamps* to *The Blue Chip Companies*. We believe the new name conveys a clearer impression of the changes that have occurred and will continue to occur in our company's activities. So long as the role of trading stamps continues to diminish in relation to our overall operations, we will increasingly seek other means of building sound value in your Blue Chip investment.

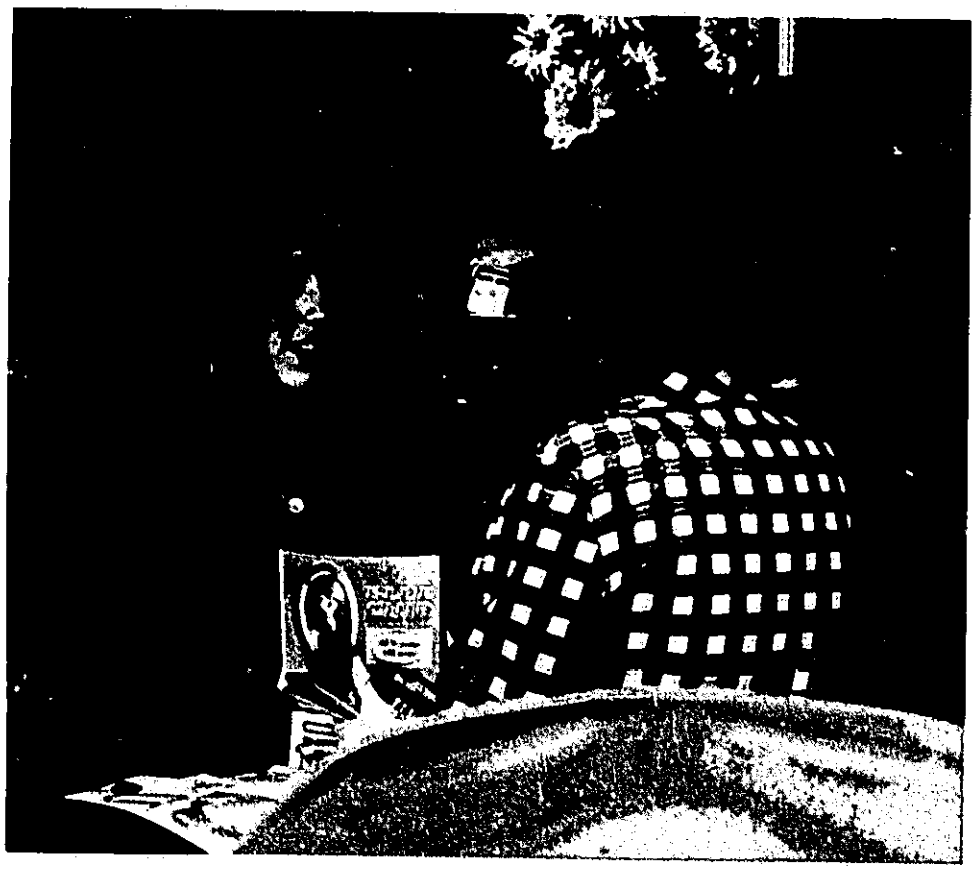
Cordially yours,

Donald A. Koeppel

Donald A. Koeppel
Chairman of the Board and President

April 12, 1974

Blue Chip's Principal Business Activities



Blue Chip Stamps derives its name from its stamp business, which started in the Sacramento area in 1956. The Company is now headquartered in Los Angeles, where its distribution center supplies merchandise to seventy-one modern, full-service redemption stores, located primarily in California. The Blue Chip trading stamp catalog is produced annually and currently offers approximately 2,000 merchandise items from 500 manufacturers.

Wesco Financial Corporation is a Pasadena-based savings and loan holding company with $450 million in assets. Wesco's wholly-owned subsidiary, Mutual Savings and Loan Association, operates at

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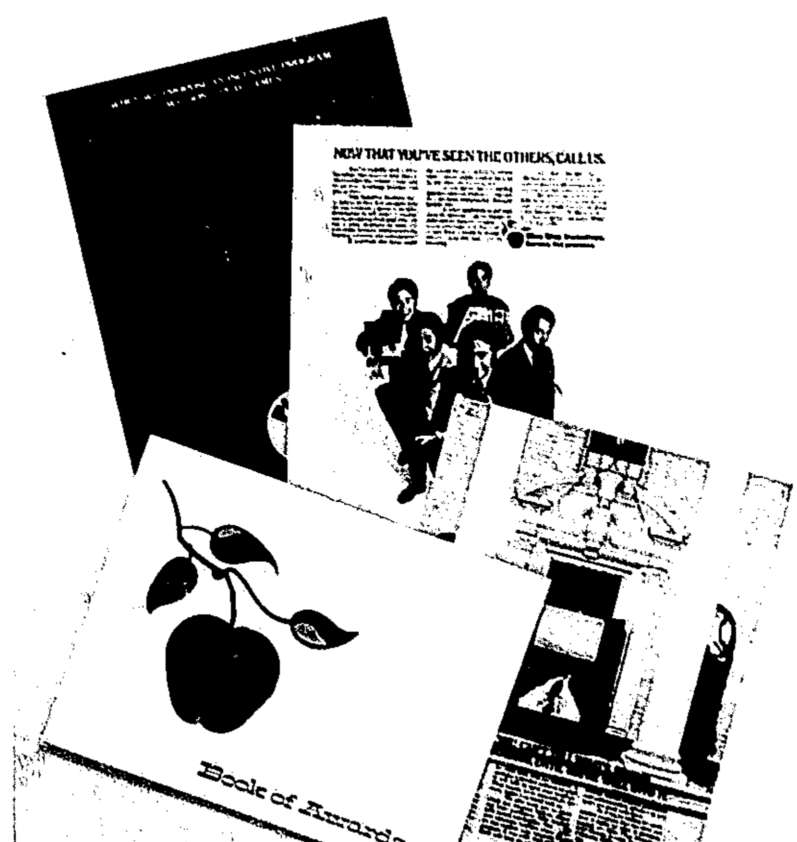
ten locations in Southern California. Three new branches are scheduled to be opened later in 1974.

See's Candy Shops, Inc. manufactures candy of the highest quality in fully equipped kitchens in Los Angeles and South San Francisco. The candy is sold fresh to the public in 172 shops in nine western states including Hawaii, all operated by See's. Three new shops are planned for completion later this fiscal year.

Blue Chip Incentives operates as a separate division on a nationwide basis. It tailors incentive programs for businesses. These programs use awards of merchandise, travel, points and stamps in order to stimulate sales or productivity, promote attendance or safety, or perform other motivational functions. The division's deluxe catalog is the cornerstone of many of these programs. In addition, Blue Chip Incentives develops, for oil companies and other large issuers of credit cards, complete merchandise packages for their credit card holders – including item selection, graphics design, mailing of promotional materials and fulfillment of merchandise orders.



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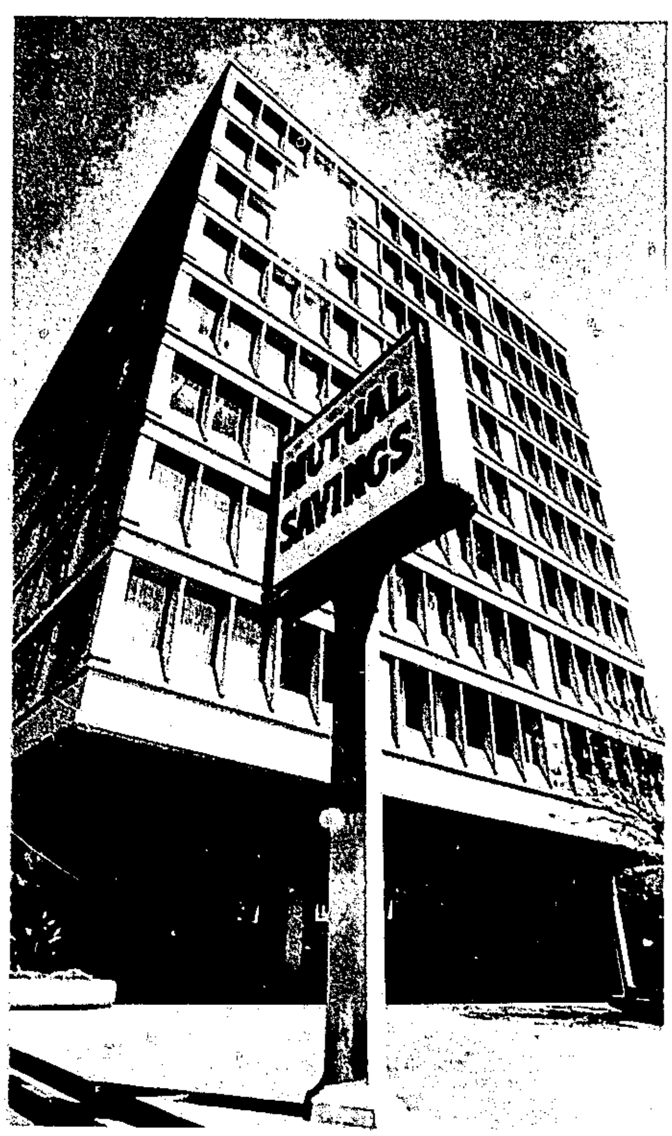
Blue Chip Stamps

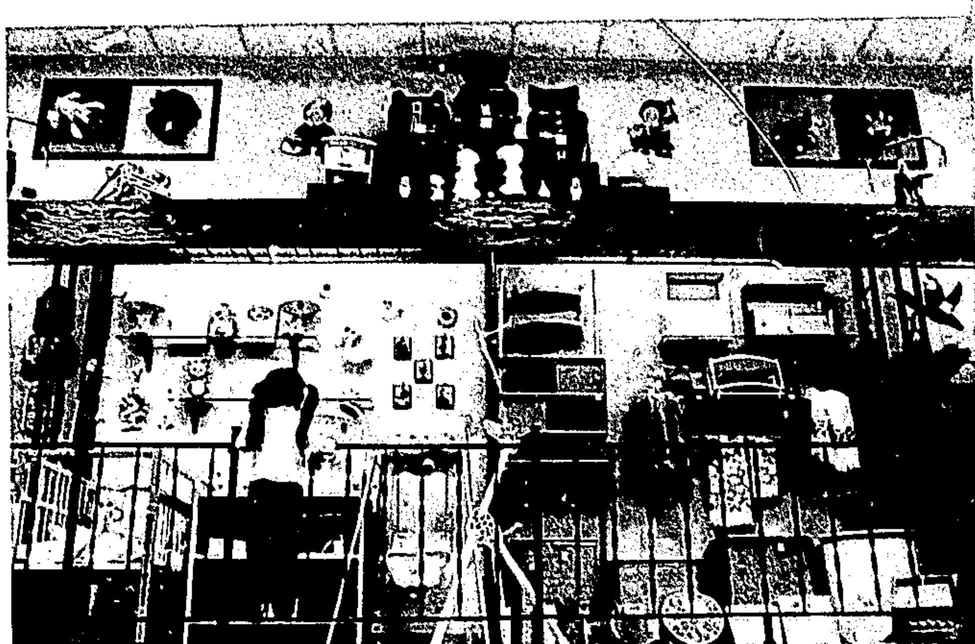
Ten-Year Summary

	3/2/74	3/3/73
Total for the Fiscal Year		
Total revenues	$102,219,000	$132,323,000
Stamp service revenues	51,375,000	88,736,000
Incentive sales	6,261,000	3,624,000
Candy sales*	35,780,000	32,049,000
Income before securities gains (losses) and extraordinary charges	8,190,000	8,108,000
Securities gains (losses)	(185,000)	(82,000)
Extraordinary charges	—	(925,000)
Net income	8,005,000	7,101,000
Total at Fiscal Year End		
Total assets	200,220,000	199,724,000
Stockholders' equity	59,887,000	53,125,000
Average Shares Outstanding**	5,179,000	5,069,000
Per Share**		
Income before securities gains (losses) and extraordinary charges	$ 1.58	$ 1.58
Net income	1.55	1.38
Book value	11.56	10.26

*From acquisition in January 1972.
**Adjusted for 5-for-1 stock split, October 1969.



3/4/72	2/27/71	2/28/70	3/1/69	3/2/68	3/4/67	2/26/66	2/27/65
$114,102,000	$127,784,000	$132,020,000	$112,151,000	$94,574,000	$94,760,000	$83,772,000	$74,256,000
100,622,000	118,374,000	124,180,000	107,602,000	91,097,000	91,209,000	81,065,000	71,969,000
2,145,000	1,759,000	1,822,000	882,000	677,000	883,000	552,000	354,000
4,104,000	—	—	—	—	—	—	—
5,907,000	8,739,000	7,738,000	5,415,000	3,333,000	4,365,000	4,444,000	2,276,000
(1,693,000)	(155,000)	27,000	229,000	85,000	(81,000)	22,000	228,000
—	—	(378,000)	(3,651,000)	—	—	—	—
4,214,000	8,584,000	7,387,000	1,993,000	3,418,000	4,284,000	4,466,000	2,504,000
190,740,000	148,422,000	147,333,000	123,796,000	95,772,000	81,999,000	77,713,000	65,207,000
46,381,000	43,296,000	35,431,000	28,049,000	23,060,000	19,487,000	15,202,000	10,736,000
5,028,000	4,957,000	4,877,000	3,530,000	3,108,000	3,108,000	3,108,000	3,108,000
$1.15	$1.72	$1.53	$1.54	$1.07	$1.41	$1.43	$ .73
.82	1.69	1.46	.57	1.10	1.38	1.44	.81
9.20	8.61	7.16	5.76	7.42	6.27	4.89	3.45



Blue Chip Stamps

Consolidated Balance Sheet

March 2, 1974 and March 3, 1973 (Note 1)

ASSETS

	1974	1973
Current assets:		
Cash	$ 3,013,000	$ 4,196,000
Marketable securities (Notes 3 and 5)	132,743,000	144,601,000
Accounts receivable	4,034,000	4,148,000
Merchandise and supplies inventories, at the lower of cost (first-in, first-out) or market	10,355,000	13,114,000
Prepaid income taxes and other expenses (Note 6)	4,879,000	4,792,000
Total current assets	155,024,000	170,851,000
Property, fixtures and equipment, at cost, less accumulated depreciation and amortization (Note 4)	10,454,000	10,785,000
Unamortized debenture discount	982,000	1,347,000
Investment in Wesco Financial Corporation (Note 1)	17,446,000	—
Excess of cost over equity in net assets of See's Candy Shops, Incorporated, less accumulated amortization (Note 1)	16,314,000	16,741,000
	$200,220,000	$199,724,000

LIABILITIES AND STOCKHOLDERS' EQUITY

	1974	1973
Current liabilities:		
Accounts payable and accrued expenses	$ 8,146,000	$ 8,626,000
Note payable to bank	—	1,000,000
Current portion of long-term debt	8,881,000	5,751,000
Income taxes payable (Note 6)	2,858,000	4,027,000
Liability for unredeemed trading stamps (Note 2)	78,776,000	93,351,000
Total current liabilities	98,661,000	112,755,000
Long-term debt, less current portion (Note 5):		
Notes payable to bank	33,000,000	23,004,000
6¾% Subordinated Debentures due 1978	8,672,000	10,840,000
Total long-term debt	41,672,000	33,844,000
Stockholders' equity (Notes 5, 7 and 11):		
Common stock, par value $1.00		
Shares authorized — 7,000,000		
Shares outstanding — 5,179,000	5,179,000	5,179,000
Paid-in capital	1,579,000	1,579,000
Retained earnings	53,129,000	46,367,000
Total stockholders' equity	59,887,000	53,125,000
	$200,220,000	$199,724,000

See accompanying notes to consolidated financial statements

Blue Chip Stamps

Consolidated Statement of Income

Fifty-two Weeks Ended March 2, 1974 and March 3, 1973 (Note 1)

	1974	1973
Revenues:		
Stamp service revenues (Note 2)	$ 51,375,000	$ 88,736,000
Incentive sales	6,261,000	3,624,000
Candy sales	35,780,000	32,049,000
Interest and dividends	8,260,000	7,315,000
Other	543,000	599,000
	102,219,000	132,323,000
Costs and expenses:		
Cost of redemptions and sales (Note 2)	68,156,000	95,662,000
Selling, general and administrative expenses	21,263,000	21,729,000
Interest and discount amortization	3,962,000	2,996,000
	93,381,000	120,387,000
Income before income taxes, equity in net income of Wesco Financial Corporation, securities losses and extraordinary charges	8,838,000	11,936,000
Provision for income taxes (Note 6)	(2,071,000)	(3,828,000)
Equity in net income of Wesco Financial Corporation (Note 1)	1,423,000	—
Income before securities losses and extraordinary charges	8,190,000	8,108,000
Securities losses, less income tax effect	(185,000)	(82,000)
Extraordinary charges (Note 11)	—	(925,000)
Net income	$ 8,005,000	$ 7,101,000
Per share (Note 8):		
Income before securities losses and extraordinary charges	$1.58	$1.58
Securities losses	(.03)	(.02)
Extraordinary charges	—	(.18)
Net income	$1.55	$1.38

Consolidated Statement of Stockholders' Equity

Fifty-two Weeks Ended March 2, 1974 and March 3, 1973 (Note 1)

	Common Stock	Paid-in Capital	Retained Earnings
Balance at March 4, 1972	$5,039,000	$ 862,000	$40,480,000
Exercise of stock options	140,000	717,000	—
Cash dividends of $.24 per share	—	—	(1,214,000)
Net income	—	—	7,101,000
Balance at March 3, 1973	5,179,000	1,579,000	46,367,000
Cash dividends of $.24 per share (Note 5)	—	—	(1,243,000)
Net income	—	—	8,005,000
Balance at March 2, 1974	$5,179,000	$1,579,000	$53,129,000

See accompanying notes to consolidated financial statements

Blue Chip Stamps

Consolidated Statement of Changes in Financial Position

Fifty-two Weeks Ended March 2, 1974 and March 3, 1973 (Note 1)

	1974	1973
Working capital was provided by:		
Income before extraordinary charges	$ 8,005,000	$ 8,026,000
Income charges (credits) not affecting working capital:		
Depreciation and amortization	1,931,000	2,141,000
Minority interest in net income of See's Candy Shops, Incorporated	22,000	35,000
Dividends received from Wesco Financial Corporation	419,000	–
Equity in net income of Wesco Financial Corporation (Note 1)	(1,423,000)	–
Working capital provided by operations	8,954,000	10,202,000
Notes payable to bank (long-term portion)	16,996,000	1,496,000
Exercise of stock options	–	857,000
Minority interest in See's Candy Shops, Incorporated	(22,000)	(1,070,000)
	25,928,000	11,485,000
Working capital was used for:		
Excess of cost over equity in net assets of See's Candy Shops, Incorporated	4,000	978,000
Property additions, net	1,022,000	1,206,000
Payment of dividends	1,243,000	1,214,000
Transfer of long-term debt to short-term debt	8,881,000	5,751,000
Debentures purchased for retirement	287,000	–
Investment in Wesco Financial Corporation (Note 1)	16,224,000	–
Extraordinary charges (Note 11)	–	925,000
	27,661,000	10,074,000
Increase (decrease) in working capital	$ (1,733,000)	$ 1,411,000
Increases (decreases) in components of working capital:		
Cash	$ (1,183,000)	$ 208,000
Marketable securities	(11,858,000)	9,870,000
Accounts receivable	(114,000)	(799,000)
Inventories	(2,759,000)	(1,073,000)
Prepaid income taxes and other expenses	87,000	735,000
Accounts payable and accrued expenses	480,000	(796,000)
Note payable to bank (short-term)	1,000,000	(1,000,000)
Current portion of long-term debt	(3,130,000)	(299,000)
Income taxes payable	1,169,000	(1,329,000)
Liability for unredeemed trading stamps	14,575,000	(4,106,000)
Increase (decrease) in working capital	$ (1,733,000)	$ 1,411,000

See accompanying notes to consolidated financial statements

Blue Chip Stamps

Notes to Consolidated Financial Statements

Note 1 – Subsidiary companies:

The consolidated financial statements include the accounts of the Company and its 99%-owned subsidiary, See's Candy Shops, Incorporated (See's). The excess of cost over equity in the net assets of See's is being amortized over 40 years; amortization amounted to $431,000 and $428,000 for the fiscal years ended in 1974 and 1973.

At March 3, 1973 the Company owned 21.9% of the outstanding shares of Wesco Financial Corporation (Wesco) common stock at a cost of $8,099,000. The Company had increased its ownership to 24.9% at April 6, 1973 and applied to federal and California regulatory authorities to obtain control of Wesco (defined *inter alia* as ownership of more than 25%). Such permission was granted in September 1973. The Company's ownership of Wesco has increased to 44.6% through March 2, 1974 and to approximately 57% through April 12, 1974. The Company's investment in Wesco is recorded at cost plus equity in net earnings for Wesco's year ended December 31, 1973; the $12,780,000 excess of equity in the net assets of Wesco over cost is being amortized over 40 years. Such amortization amounted to $218,000 during the fiscal year ended in 1974. Summarized financial information of Wesco for the year ended December 31, 1973 follows:

Assets –	
Cash and marketable securities	$ 40,112,000
Loans receivable, less unearned loan fees, unrealized profit and loans in process	389,584,000
Other assets	22,284,000
Total assets	$451,980,000
Liabilities and stockholders' equity –	
Savings deposits	$345,530,000
Other liabilities	38,899,000
Total liabilities	384,429,000
Stockholders' equity	67,551,000
Total liabilities and stockholders' equity	$451,980,000
Total income	$ 34,289,000
Net earnings	$ 4,608,000
Per share	$1.94

Note 2 – Stamp service accounting:

The Company recognizes stamp service revenues upon issuance of its trading stamps and provides a liability account for unredeemed trading stamps consisting of the cost of merchandise and related redemption expenses. For a number of years the Company has made statistical evaluations of its redemptions. Based upon analysis of such evaluations, the Company presently estimates that 97.5% of all stamps issued will ultimately be redeemed. The liability for unredeemed trading stamps of $78,776,000 at March 2, 1974 included $64,431,000 for the cost of merchandise and $14,345,000 for redemption expenses.

Note 3 – Marketable securities:

Following is a summary of marketable securities, which are stated at cost:

	Cost	Market Value
March 2, 1974 –		
Short-term investments	$ 31,164,000	$ 31,183,000
Preferred and common stocks	101,579,000	97,471,000
	$132,743,000	$128,654,000
March 3, 1973 –		
Short-term investments	$ 21,298,000	$ 21,298,000
Preferred and common stocks	123,303,000	127,004,000
	$144,601,000	$148,302,000

Note 4 – Property, fixtures and equipment:

Following is a summary of property, fixtures and equipment:

	March 2, 1974	March 3, 1973
Land	$ 2,900,000	$ 2,900,000
Buildings	5,755,000	5,703,000
Furniture, fixtures and equipment	9,289,000	8,957,000
Leasehold improvements	4,287,000	4,116,000
	22,231,000	21,676,000
Less accumulated depreciation and amortization	11,777,000	10,891,000
	$10,454,000	$10,785,000

Depreciation and amortization of property, fixtures and equipment are provided by straight line and accelerated methods over the estimated useful lives of the assets. Total provisions amounted to $1,353,000 and $1,354,000 for the fiscal years ended in 1974 and 1973.

Notes to Consolidated Financial Statements (Cont.)

Note 5 – Long-term debt:

In January 1974 the Company refinanced a bank loan of $28,755,000 and obtained $11,245,000 in additional funds. The resulting bank loans at March 2, 1974 aggregating $40,000,000 are repayable beginning January 1975 in annual installments of $7,000,000 through 1978 and $6,000,000 in 1979 and 1980. Interest is payable monthly at one-half to one per cent above prime rate. In addition to the stock of See's and Wesco, securities having an aggregate market value of approximately two-thirds the unpaid balance are pledged as collateral. Under the most restrictive covenants of the loan agreements, total unsubordinated long-term debt (including the loans) may not exceed the sum of stockholders' equity and subordinated debt, and the Company's current liabilities may not exceed the aggregate of cash, unrestricted marketable securities and merchandise inventory.

The debentures are subordinated to senior indebtedness as defined in the underlying indenture. At least 20% of the debentures must be paid to a sinking fund annually beginning December 1, 1974, and the Company may redeem debentures after December 1, 1974. Under the terms of the indenture, the Company is permitted to pay cash dividends in any fiscal year in an amount not to exceed the greater of (a) 24 cents per share or (b) 25% of the net income for the preceding fiscal year. Dividends may not be paid if the Company is in arrears in any sinking fund payments. During the fiscal year ended in 1974 the Company purchased $287,000 principal amount of debentures for retirement.

Note 6 – Income taxes:

The income tax provision of $2,071,000 for the fiscal year ended in 1974 was 23.4% of pretax income of $8,838,000. Following is a summary of the differences between the federal statutory rate and this effective percentage:

Statutory income tax rate	48.0%
Dividend exclusion	(27.7)
State income taxes, net of federal income tax benefit	3.8
All other (net)	(.7)
Effective income tax rate	23.4%

Prepaid income taxes of $3,815,000 and $3,802,000 at March 2, 1974 and March 3, 1973 result primarily from deducting certain redemption expenses for income tax reporting purposes when stamps are redeemed and for financial reporting purposes when stamps are issued. The net increase in prepaid income taxes resulting from timing differences amounted to $13,000 and $851,000 for the fiscal years ended in 1974 and 1973.

At March 2, 1974 the Company had capital loss carry-forwards of $1,883,000 available for offset against capital gains of $1,300,000 and $583,000 through fiscal years ending in 1977 and 1979.

Investment tax credits, which have not been material, are recognized as the tax benefits are realized.

In 1972 the Company received a notice of deficiency from the Internal Revenue Service claiming additional taxes of approximately $7,500,000, excluding interest, for the three fiscal years ended in 1971. Of this amount, more than $5,500,000 results from the Service's contention that the Company has overstated its liability for unredeemed stamps by overestimating the number of stamps issued which will ultimately be redeemed. Since its inception in 1956, the Company's financial statements and tax returns have been prepared on the basis that 97.5% of all stamps issued will ultimately be redeemed. This percentage has been based upon annual statistical evaluations of stamp redemptions. The Company disagrees with the Service's position and accordingly has petitioned the United States Tax Court for a determination that there are no additional federal income taxes due for the fiscal year ended in 1971 and prior years. The other items in the notice involved the disallowance of certain expenses and were settled in January 1974 for approximately $200,000. The California Franchise Tax Board proposed assessment of additional taxes based on the federal notice, and the Company filed a protest.

Note 7 – Stock options:

Under the Company's qualified stock option plan, options to purchase shares of the Company's common stock were outstanding at March 2, 1974, as follows: 7,200 shares at $14.75 (including 5,325 currently exercisable) and 18,000 shares at $15.1875 (of which 4,500 were currently exercisable). No options were granted or exercised during the fiscal year.

Note 8 — Per share computations:

Per share amounts are based upon the weighted average number of shares of common stock outstanding during the fiscal year adjusted for the dilutive effect of outstanding stock options.

Note 9 — Pension plan:

The Company has a noncontributory pension plan which covers employees meeting certain eligibility requirements. The plan is funded annually and the cost for the fiscal years ended in 1974 and 1973 approximated $120,000 and $300,000. There are no unfunded prior service costs.

Note 10 — Lease commitments and rental expense:

At March 2, 1974 minimum rental commitments are as follows:

Fiscal year ending in—	
1975	$2,662,000
1976	2,289,000
1977	1,782,000
1978	1,455,000
1979	1,282,000
Five fiscal years ending in—	
1984	3,428,000
1989	988,000
1994	253,000

The net rental expense was $3,708,000 and $3,645,000 for the fiscal years ended in 1974 and 1973. Rentals applicable to candy operations are generally determined on the basis of a fixed percentage of sales subject to a specific minimum rental. Such minimum rental expense, which is included above, was $834,000 and $790,000 for the fiscal years ended in 1974 and 1973.

Note 11 — Legal proceedings:

During the fiscal year ended in 1973, the Company settled eleven lawsuits for $1,923,000. The settlements, less $998,000 applicable income taxes, were charged against income as extraordinary charges.

Pursuant to a consent final judgment entered in 1967, the Company in June 1972 submitted for approval by the United States District Court a plan to offer for sale one third of its California trading stamp business located within a contiguous geographical area in Southern California. In January 1973, the Court made an order (1) disapproving said plan, (2) requiring the Company to continue efforts to negotiate a sale and (3) calling for the appointment of an independent expert to study the feasibility of a sale or spin-off of a portion of the Company's trading stamp business under existing conditions. The report of the independent expert has not yet been filed with the Court. The Company believes that such a sale or spin-off, if consummated under existing market conditions, would compel the Company to discontinue issuance of its trading stamps.

The Company is a defendant in a purported class action filed March 1, 1971 to recover for stamp savers monies collected by it as reimbursement for California sales taxes on redemption of stamps. Plaintiffs claim that redemption transactions are not taxable and that all such collections should be returned, or alternatively, that such collections exceeded the tax properly payable and such excess should be returned. The Company has paid sales taxes to the state equal to its reimbursement collections. The Company has asserted claims against the state for reimbursement of all or part of any recovery by plaintiffs. Following denial of these claims by the state, the Company cross-complained against the state seeking indemnity. The original complaint was amended to assert fraud and to seek punitive damages. On June 1, 1973 two partial summary judgments were entered by way of interlocutory orders, neither of which has yet become final or appealable. The first was in favor of the Company to the effect that the redemption transactions were taxable. The second was in favor of plaintiffs to the effect that the Company's collections exceeded the tax properly payable. In the opinion of counsel for the Company the second partial summary judgment was erroneous. Issues relating to the class action aspects of the case remain unresolved along with a number of issues of fact. Maximum liability in respect of this action is estimated at $7,000,000 less the amount of any money which may be recovered on the claims against the state. Counsel believes the prospects for such recovery to be good. In the opinion of counsel for the Company, substantial defenses are available, but counsel cannot predict the ultimate outcome of the action.

A purported class action was filed on November 10, 1970 against the Company and certain of its present and former

Notes to Consolidated Financial Statements (Cont.)

stockholders and directors. The complaint was filed on behalf of retailer users of Blue Chip stamps who failed to purchase stock of the Company in a 1968 offering to retailer users. The complaint alleges damages to plaintiffs of $21,400,000, together with exemplary damages of $25,000,000, interest, attorneys' fees and costs, and prays that plaintiffs have the right to purchase stock, or units of stock and debentures, of the Company on the terms of the 1968 offering. The action was dismissed with prejudice by the United States District Court. On October 15, 1973 a panel of three judges of the United States Court of Appeals for the Ninth Circuit reversed the prior dismissal by the District Court and remanded the case for further proceedings. In a two-to-one opinion, the panel held that a class of persons who were entitled to but failed to purchase securities of the Company in connection with the 1968 offering had standing to sue for damages under Rule 10b-5 of the Securities Exchange Act of 1934, if they could prove that such failure to purchase was induced by alleged fraudulent representations of the Company and certain of its past and present officers, directors and shareholders. On April 1, 1974 the Ninth Circuit denied a petition for rehearing and a request that the case be heard by the entire panel of judges of the Ninth Circuit. The defendants will seek a review by the United States Supreme Court. On June 21, 1971 plaintiffs filed a substantially identical action against the same defendants in the Los Angeles County Superior Court, but the Company has not yet been served with process in that action. In the opinion of counsel for the Company, upon the facts now known and the present state of the law, there appear to be substantial defenses on the merits to the complaints in both the federal and state actions.

The Company, together with a number of oil companies and supermarket chains, was named as defendant in an antitrust action filed on July 12, 1971 by a California corporation formerly engaged in the trading stamp business. The complaint seeks treble damages in substantial amounts plus attorneys' fees and costs. The Company has not been served with process. In the opinion of counsel for the Company, upon the facts known, the action is without substantial merit.

Report of Independent Accountants

To the Board of Directors and
Stockholders of Blue Chip Stamps

We have examined the consolidated balance sheet of Blue Chip Stamps and its consolidated subsidiary as of March 2, 1974 and March 3, 1973, and the related consolidated statements of income, stockholders' equity and changes in financial position for the fiscal years then ended. 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. We did not examine the financial statements of Wesco Financial Corporation which is accounted for on the equity method in the consolidated financial statements (Note 1). These statements were examined by other independent accountants whose report thereon has been furnished to us. Our opinion expressed herein, insofar as it relates to the amounts included for Wesco Financial Corporation, is based solely upon such report.

As explained in Note 11 to the accompanying financial statements, the Company is subject to certain legal proceedings.

In our opinion, based on our examinations and the report of other independent accountants, subject to the effect, if any, of the legal proceedings referred to in the preceding paragraph, the consolidated financial statements present fairly the financial position of Blue Chip Stamps and its consolidated subsidiary at March 2, 1974 and March 3, 1973 and the results of their operations and changes in financial position for the fiscal years then ended, in conformity with generally accepted accounting principles consistently applied.

Price Waterhouse & Co.
Price Waterhouse & Co.

Los Angeles, California
April 12, 1974

Directors and Officers

DIRECTORS

Warren E. Buffett
Personal Investments; Chairman of the Board of Berkshire Hathaway Inc. and of Diversified Retailing Company, Inc.

Z. Wayne Griffin
Personal investments; real estate development

John F. Guerin, Jr.
General partner of J. P. Guerin & Co., Investors; Chairman of the Board of Governors of Pacific Stock Exchange, Inc.

Joseph P. Hughes
President of Hughes Markets, Inc.; a director of Certified Grocers of California, Ltd.

Emmett H. Jones
President of Terminal Oil Company, Industrial Engineering & Equipment Corporation and Westates Investment Co.

Donald A. Koeppel
Chairman of the Board and President of the Company

Charles T. Munger
General partner of Wheeler, Munger & Co., Investors

William F. Ramsey
Executive Vice President of the Company

Ron Stever
Chairman of the Board of The Stever Companies, consulting actuaries and insurance brokers, and of Crescent Wharf & Warehouse Co.

Andrew J. Wolf
President of A & B Supermarkets, Inc.

OFFICERS

Donald A. Koeppel
Chairman of the Board and President

William F. Ramsey
Executive Vice President

Raymond H. Allen
Vice President, Information Systems

Gerald N. Anderson
Vice President, Sales

Robert H. Bird
Vice President, Secretary and Treasurer

James D. Carter
Vice President, Operations

Walter M. Cusack
Vice President, Incentives

William K. Klepper
Vice President, Merchandise

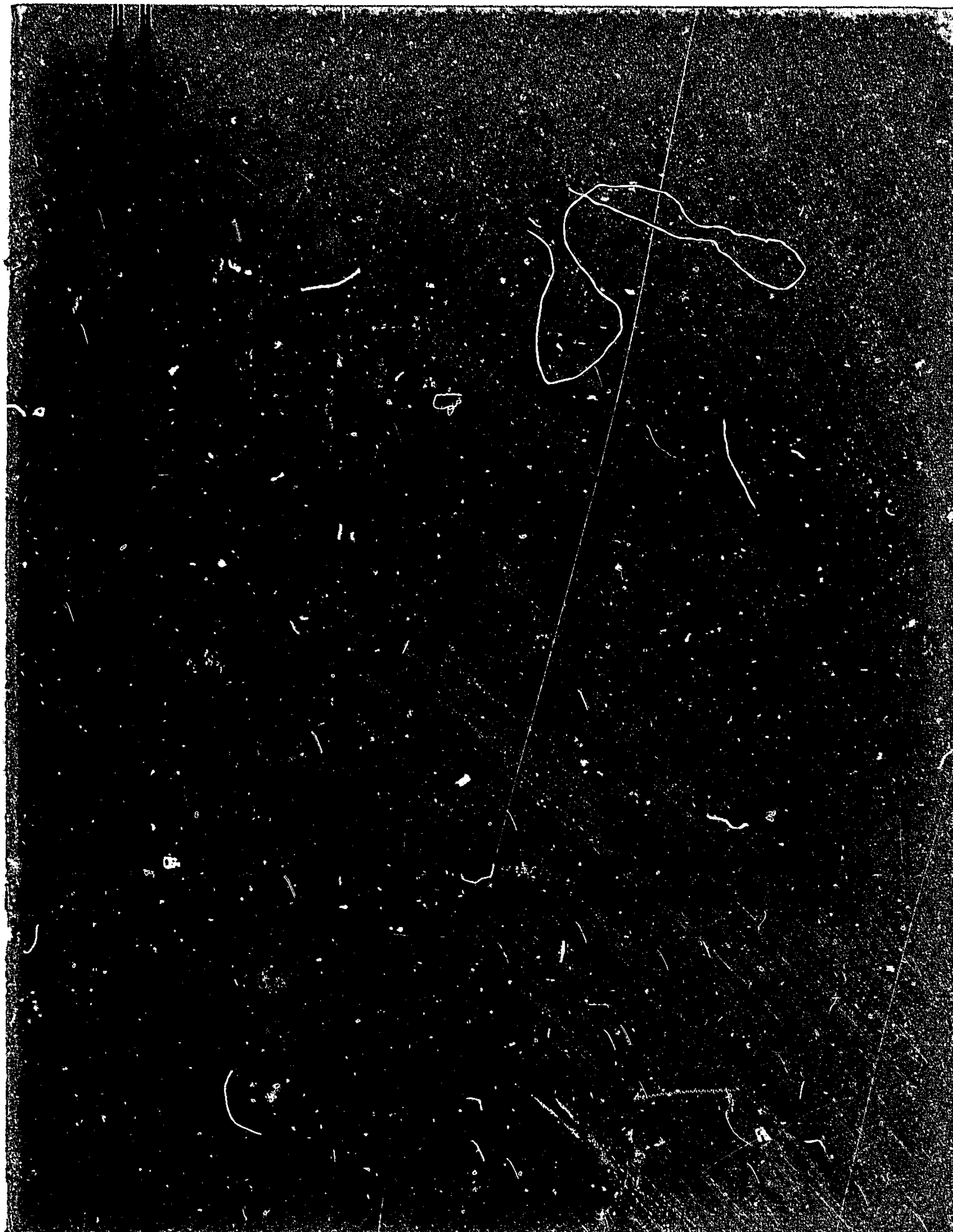
Kenneth E. Wittmeyer
Vice President, Industrial Relations

Ernest P. Paulson
Controller and Assistant Secretary

TRANSFER AGENTS AND REGISTRARS

Bank of America, N.T.& S.A.
San Francisco

Bankers Trust Company
New York



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Berkshire Hathaway Inc.

To the Stockholders of
Berkshire Hathaway Inc.:

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

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

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

Textile Operations

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

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

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

Insurance Operations

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

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

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

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

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

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

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

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

Banking Operations

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

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

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

Merger With Diversified Retailing Company, Inc.

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

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

Blue Chip Stamps

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

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

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

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

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

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

Sun Newspapers, Inc.

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

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

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

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

Warren E. Buffett
Chairman of the Board

March 29, 1974

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

The Board of Directors and Stockholders
Berkshire Hathaway Inc.:

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

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

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

Peat, Marwick, Mitchell & Co.

March 20, 1974

Berkshire Hathaway Inc.

AND

Consolidated Subsidiaries

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 29, 1973 and December 30, 1972

ASSETS	Dec. 29, 1973	Dec. 30, 1972
Cash	$ 2,885,645	$ 4,998,225
Investments:		
Bonds (note 2)	74,474,461	88,148,480
Preferred stocks (note 3)	2,298,348	2,942,252
Common stocks of unaffiliated companies (note 3)	49,756,778	17,411,780
Common stock of Blue Chip Stamps (note 4)	13,717,274	11,287,396
Unconsolidated bank subsidiary (note 5)	21,003,034	20,472,590
Other unconsolidated subsidiaries (note 5)	1,333,832	1,258,832
Accounts receivable from customers, agents and others (less allowance for doubtful accounts, 1973 — $332,679; 1972 — $226,530)	14,056,574	12,853,881
Inventories (note 6)	7,136,676	6,827,043
Real estate, equipment, furniture and leasehold improvements, at cost less allowance for depreciation and amortization (note 7)	3,668,005	3,640,249
Deferred insurance premium acquisition costs	5,240,000	5,624,000
Other assets	560,987	645,105
	$196,131,614	$176,109,833

LIABILITIES AND STOCKHOLDERS' EQUITY		
Losses and loss adjustment expenses	$ 61,675,768	$ 60,275,018
Unearned premiums	21,281,980	23,839,397
Funds held under reinsurance treaties	1,318,205	957,845
Agents' and policyholders' deposits	471,728	540,742
Amounts due for purchase of securities	459,609	674,123
Accounts payable and accrued expenses	4,726,609	4,383,758
Income taxes:		
Current	262,357	3,576,109
Deferred	3,297,368	3,214,084
7½% debentures due 1987 (note 8)	598,540	641,300
Notes payable to banks (note 9)	—	9,000,000
8% senior notes due 1993 (note 10)	20,000,000	—
Excess of net assets of consolidated subsidiaries over cost of investment	579,070	579,070
Other liabilities	304,914	133,364
	114,976,148	107,814,810
Stockholders' equity:		
Common stock of $5 par value. Authorized at December 29, 1973, 1,100,000 shares, December 30, 1972, 1,722,983 shares; issued at December 29, 1973, 979,569 shares, December 30, 1972, 1,017,547 shares	4,897,845	5,087,735
Retained earnings (note 10)	76,257,621	64,024,663
	81,155,466	69,112,398
Less, at December 30, 1972, cost of 37,978 shares of common stock in treasury	—	817,375
Total stockholders' equity	81,155,466	68,295,023
Contingencies (notes 12 and 14)		
	$196,131,614	$176,109,833

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS
52 weeks ended December 29, 1973 and December 30, 1972

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

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

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

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

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 29, 1973 and December 30, 1972

(1) **Summary of Significant Accounting Policies and Practices**

(a) Basis of Presentation

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

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

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

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

(b) Investment in Securities, Other than Affiliates

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

(c) Investment in Blue Chip Stamps

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

(d) Insurance Premiums

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

(e) Reserve for Losses

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

(f) Catastrophe Reserves

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

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

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

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(h) Inventories

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

(i) Income Taxes

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

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

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

(2) Bonds Deposited with Others

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

(3) Investments in Stocks of Unaffiliated Companies

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

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

(4) Investment in Blue Chip Stamps

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

The investment in Blue Chip is summarized as follows:

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

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

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

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

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS, *Continued*

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

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

BLUE CHIP STAMPS
Consolidated Balance Sheets
($000 omitted)

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

BLUE CHIP STAMPS
Consolidated Earnings Summaries
($000 omitted)

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

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

(5) Investments in Unconsolidated Subsidiaries

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

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

(6) Inventories

A summary of inventories follows:

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

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

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

The composition of plant and equipment is shown below:

December 29, 1973	*Properties of textile operations*	*Properties of insurance group*	*Total*
Land	$ 84,860	$ 83,847	$ 168,707
Buildings	2,364,265	1,251,905	3,616,170
Machinery and equipment	12,361,378	—	12,361,378
Furniture and fixtures and leasehold improvements	593,900	935,745	1,529,645
	15,404,403	2,271,497	17,675,900
Less accumulated depreciation and amortization	13,341,570	666,325	14,007,895
	$ 2,062,833	$ 1,605,172	$ 3,668,005
December 30, 1972			
Land	$ 84,860	$ 83,847	$ 168,707
Buildings	2,344,684	1,172,156	3,516,840
Machinery and equipment	11,869,465	—	11.369,465
Furniture and fixtures and leasehold improvements	660,867	964,793	1,625,660
	14,959,876	2,220,796	17,180,672
Less accumulated depreciation and amortization	12,993,741	546,682	13,540,423
	$ 1,966,135	$ 1,674,114	$ 3,640,249

(8) 7½% Subordinated Debentures

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

(9) Notes Payable to Banks

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

(10) 8% Senior Notes Due 1993

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

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

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

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

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

(11) Income Taxes

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

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

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

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

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

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

(12) "One-Bank Holding Company" Status

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

(13) "Savings and Loan Holding Company" Status

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

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(14) Proposed Merger

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

Berkshire Hathaway Inc.

INSURANCE GROUP

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF ASSETS AND LIABILITIES

December 31, 1973 and 1972

ASSETS

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

LIABILITIES, CAPITAL STOCK AND SURPLUS

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

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF INCOME AND REALIZED INVESTMENT GAINS

Years ended December 31, 1973 and 1972

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

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

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

PAID-IN SURPLUS

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

UNASSIGNED SURPLUS

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

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF CHANGES IN FINANCIAL POSITION

Years ended December 31, 1973 and 1972

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

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

NOTES TO FINANCIAL STATEMENTS

December 31, 1973 and 1972

(A) Note References

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

(B) Basis of Presentation

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

(C) Stockholders' Equity

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

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

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

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

(D) Federal Income Taxes

Federal income tax expense is made up of the following:

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

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

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

Berkshire Hathaway Inc.

BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford

Financial Statements
1973 and 1972

Berkshire Hathaway Inc.
BANK SUBSIDIARY

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

CONSOLIDATED BALANCE SHEETS
December 31, 1973 and 1972

ASSETS

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

LIABILITIES AND STOCKHOLDERS' EQUITY

	1973	1972
Demand deposits	$ 55,716,465	$ 55,129,900
Time deposits	81,450,028	77,558,396
Total deposits	137,166,493	132,688,296
Accrued taxes and other liabilities (note 5)	835,154	886,645
Total liabilities	138,001,647	133,574,941
Allowance for possible loan losses (note 6)	1,163,658	1,024,601
Stockholders' equity:		
Common stock, $20 par value. Authorized and issued 250,000 shares	5,000,000	5,000,000
Surplus	5,000,000	5,000,000
Undivided profits	8,238,029	7,796,349
Reserve for contingencies	1,001,000	1,001,000
Total stockholders' equity	19,239,029	18,797,349
	$158,404,334	$153,396,891

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

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

CONSOLIDATED STATEMENTS OF INCOME
Years ended December 31, 1973 and 1972

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

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY

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

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

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

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

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

See accompanying notes to consolidated financial statements of Bank Subsidiary.

Berkshire Hathaway Inc.
BANK SUBSIDIARY
The Illinois National Bank & Trust Co. of Rockford
AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 1973 and 1972

(1) Significant Accounting Policies

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

(a) Consolidation

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

(b) Investment Securities

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

(c) Installment Loans

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

(d) Bank Premises and Equipment

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

(e) Federal Income Taxes

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

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

(2) Investment Securities

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

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

(3) Loans

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

(4) Bank Premises and Equipment

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

(5) Accrued Taxes and Other Liabilities

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

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

The components of consolidated income tax expense are as follows:

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

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

Berkshire Hathaway Inc.
BANK SUBSIDIARY

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

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

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

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

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

(6) Allowance for Possible Loan Losses

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

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

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

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

(7) Pension and Profit-Sharing Plan

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

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

PEAT, MARWICK, MITCHELL & CO.
CERTIFIED PUBLIC ACCOUNTANTS
200 WEST STATE STREET, SUITE 700
ROCKFORD, ILLINOIS 61101

The Board of Directors and Stockholders
The Illinois National Bank & Trust Co. of Rockford:

We have examined the consolidated balance sheets of The Illinois National Bank & Trust Co. of Rockford and subsidiary as of December 31, 1973 and 1972, and the related consolidated statements of income, stockholders' equity and changes in financial position for the years 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 aforementioned consolidated financial statements present fairly the financial position of The Illinois National Bank & Trust Co. of Rockford and subsidiary at December 31, 1973 and 1972, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

January 18, 1974