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DIVERSIFIED RETAILING CO INC

10-K

OTHER 1975

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: 2/2/74 Rec: 5/3/74
Auditor: Ernst & Ernst
Shareholders: 288

For the years ended:	2/2/74	2/3/73
Revenues:	$38,398,636	$38,918,071
Earnings:	$2,982,254/$2.98	$2,918,042/$2.92
Extr. Items:	$395,578	$193,021
Assets:	$31,096,007	$27,855,906
Net Worth:	$20,902,749	$17,920,495

Description of Business: Operates chain of retail stores selling women's and children's apparel in Chicago, Milwaukee, Philadelphia and Chester, Pa. Engages in acceptance of portions of insurance contracts.

- Chain store operation; Womens apparel retailing; Childrens apparel retailing
- Reinsuring insurance companies

Auditor's Report:

- Qualified opinions for uncertainties; Litigation; Affiliated companies/; Proposed divestiture; Forced divestiture; Consent decrees; Trading stamp companies
- Qualified opinions for uncertainties; Litigation; Affiliated companies/; Class action; Rescission; Sales taxes; Trading stamp companies
- Qualified opinions for uncertainties; Affiliated companies/; Class action; Private placement; Stock offering; Appealed court cases

Financial Statements and Notes:

- Goodwill amortized under 40 years
- Subsidiary fiscal year variations; Unconsolidated insurance subs
- Accounting estimate changes; Useful life; Goodwill; Investees; *Blue Chip Stamps; Goodwill amortized under 40 years
- Unusual effective tax rate; Intangible asset amortization method; Goodwill
- Unusual effective tax rate; Dividends received deductions (IRC)
- Extraordinary gains; Condemnation; Real estate disposal; Eminent domain
- Equity method of carrying investment; Less than 20 percent owned companies; *Blue Chip Stamps; Investees

Exhibits: None indexed

10-Q For: 5/4/74 Rec: 6/18/74
10-Q For: 8/3/74
10-Q For: 11/2/74

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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 1, 1975

Commission file number:
2-27473

DIVERSIFIED RETAILING COMPANY, INC.

State of Incorporation: Maryland

I.R.S. Employer Identification No.
52-0846359

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 shares of Berkshire Hathaway Inc.; subsidiaries of the Company also own shares of Berkshire Hathaway Inc.

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.

On March 15, 1974, the Directors of the Company approved in principal the proposed merger of the Company with and into Berkshire Hathaway Inc. (hereinafter referred to as "Berkshire"), a Delaware corporation. On January 28, 1975, the Directors of the Company determined to abandon the proposed merger.

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,

NOTE: Unless the text otherwise indicates, all statements made in PART I describe circumstances existing as of February 1, 1975.

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 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 re chasing 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.

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 1, 1975, 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 operated stores in Philadelphia, Pennsylvania, have been the subject of condemnation proceedings. A lease to one of the stores was terminated effective April 20, 1974, and operations in the other store were terminated in June, 1974. In the fiscal years ended February 2, 1974 and February 1, 1975, respectively, gross sales from these were approximately $2,531,000.00 (6.8% of total sales) and $852,000.00 (2.4% of total sales).

In addition to operating the chain of retail stores, Associated wholly owns three (3) subsidiaries, and one of those subsidiaries owns 99.6% of another company:

(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. Anbac has no employees.

(3) Columbia Insurance Company

Columbia Insurance Company* (hereinafter referred to as "Columbia"), a Nebraska corporation, is a wholly-owned subsidiary of Associated which engages in the business of fire and casualty insurance and reinsurance. 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 fifteen (15) other states. At present, Columbia's business consists primarily 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").

National Indemnity is a wholly-owned subsidiary of Berkshire. Although as of February 1, 1975, 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 ITEM 4. PARENTS AND SUBSIDIARIES and ITEM 12. DIRECTORS OF REGISTRANT), 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 principal source of business. Columbia currently is 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.

(4) Southern Casualty Insurance Company

On April 30, 1974 Columbia purchased 99.6% of the issued

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* Formerly "Reinsurance Corp. of Nebraska".

and outstanding voting securities of Southern Casualty Insurance Company (hereinafter referred to as "Southern"). Southern is licensed to write workmen's compensation coverage in the State of Louisiana.

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

The Company, through subsidiaries, actively conducts only one significant line of business, i.e., retailing of women's and children's apparel. Insurance and reinsurance operations, commenced in the Company's fiscal year ended January 30, 1971 through Columbia, have never been significant as defined for purposes of this Item if Columbia's equity in undistributed earnings of affiliated companies, not recognized by State insurance department regulatory authorities, are not considered as derived from insurance operations.

The Company and its consolidated subsidiaries (including Columbia) have investments in Berkshire Hathaway Inc. and Blue Chip Stamps which are accounted for by the equity method. Although these investments are not considered lines of business, earnings attributable to the holdings contribute significantly to consolidated net income as revealed in Item 2 following.

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ITEM 2. SUMMARY OF OPERATIONS.

This summary [illegible]ould be read in con[illegible] with the financial statements and notes thereto [illegible] in Item 10(a).

	Fiscal Year Ended				
	January 30, 1971	January 29, 1972	February 3, 1973*	February 2, 1974	February 1, 1975
	(In thousands of dollars except per share amounts)				
Net sales	39,832	38,598	38,918	38,399	34,925
Gross profit	13,388	12,910	13,490	13,376	13,096
Interest and financing costs	647	673	687	720	677
Income taxes applicable to operating earnings	1,227	733	704	441	307
Earnings before equity in earnings of other companies, gain (loss) from sales of securities and extraordinary items	1,283	703	751	576	403
Equity in earnings of other companies, net of taxes	437	724	1,972	1,985	1,582
Realized gains (losses) from sales of securities less applicable taxes	--	200	195 (b)	26	(210)
Earnings before extraordinary items	1,720	1,627	2,918	2,587	1,775
Extraordinary gains (losses), less applicable taxes	--	(111) (a)	-- (b)	395	68
Net earnings	1,720	1,516	2,918	2,982	1,843
Net earnings per share (1,000,000 shares outstanding)	$1.72	$1.52	$2.92	$2.98	$1.84
Cash dividends per share	NONE	NONE	NONE	NONE	NONE

* The fiscal year ended February 3, 1973 consisted of 53 weeks.

This summary includes the results of operations of Columbia Insurance Company, a previously unconsolidated subsidiary. Prior year amounts have been restated to conform to this consolidated presentation, with no change in net earnings.

(a) The extraordinary loss for fiscal 1972 resulted from additional income taxes related to the sale of a subsidiary in fiscal 1970.

(b) A gain on the exchange of securities of $193,000 was originally reported as an extraordinary item. To conform to the presentation resulting from the consolidation mentioned above, this gain has been included with realized securities gains in this summary.

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

MANAGEMENT'S DISCUSSION OF SUMMARY OF OPERATIONS.

Net sales declined in the latest fiscal year by $3,474,000, or approximately 9% from the preceding year. Although four stores were opened by Associated during the year, sales from these new units did not offset the loss of sales from five stores which were closed; the net decline in sales from stores opened/closed was $1,446,000. The remaining decline of $2,028,000 resulted from a general decline (approximately 6%) in sales of the 65 units open during both years.

The decline in sales caused a decline in gross profits of $280,000, or 2%, from that of the prior year. A combination of factors including a more favorable product mix, increased opportunity for purchase of vendors promotional items and somewhat improved selling prices prevented a greater decline in gross profit.

Income taxes applicable to consolidated operating earnings have been as follows for the past three years.

	Fiscal Year Ended		
	February 3, 1973	February 2, 1974	February 1, 1975
State and local income taxes	$255,000	139,000	166,000
Federal income taxes	449,000	302,000	141,000
	$704,000	441,000	307,000

State and local income taxes vary from year to year as a combined result of varying laws between the numerous jurisdictions in which the companies operate and the varying operating results within those jurisdictions. Federal income taxes have declined from the preceding year for each of the past two years as a result of declining taxable operating earnings, while non-taxable income items have remained relatively constant.

Equity in earnings of other companies declined in the most recent fiscal year, reflecting principally a 45% decline from 1973 in Berkshire's reported earnings for 1974.

The realized loss from sale of securities, less applicable tax benefit, in the most recent fiscal year represents recognition by Columbia of a provision for anticipated losses in its common stock portfolio. The realized gain from sale of securities, less applicable capital gains tax, in the fiscal year ended February 2, 1974, resulted from a gain realized by Associated less a loss realized by Columbia on disposition by them of certain common stock of an unaffiliated company (New Yorker Magazine). In March of 1972, Associated exchanged certain investment securities it then held for 300,000 shares of common stock of Blue Chip Stamps. The transaction was a taxable exchange and the gain less taxes applicable to the transaction is reflected in the summary of earnings in the third preceding year as a realized gain from sale of securities. At February 1, 1975, marketable securities were held only by insurance subsidiaries of the Company. (Shares held of Berkshire Hathaway Inc. and Blue Chip Stamps are not viewed by management as marketable securities - it is the Company's intention to hold these shares indefinitely as permanent investments.)

The extraordinary gains reflected for each of the past two years resulted from condemnation proceeds received for certain Philadelphia properties of Associated, as more fully set forth in Note M to the consolidated financial statements.

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 seven (7) of its store locations, all of which are in Chicago, Milwaukee, Philadelphia, Chester, Pennsylvania and Gary, Indiana. Another location, previously owned by Associated, 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. The aggregate annual minimum rental paid by Associated during the fiscal year ended February 1, 1975 for the store locations which it leases was approximately $1,575,000. 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. (See Note K of the Notes to CONSOLIDATED FINANCIAL STATEMENTS.)

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 supervised 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 1, 1975, Warren E. Buffett owned 39.9%* of the Company's common stock; First Manhattan Co. (of which David S. Cottesman 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 three subsidiaries: Anbec, Inc., an Illinois corporation; Columbia Insurance Company, a Nebraska corporation; and Fashion Outlet of Michigan, Inc., a Michigan corporation. Columbia owns 99.6% of Southern. All of the above-named subsidiaries are included in the consolidated financial statements of the Company.

As of February 1, 1975, the Company, through its subsidiaries, Associated and Columbia, beneficially owned approximately sixteen percent (16%) of the common stock of Blue Chip Stamps (hereinafter referred to as "Blue Chip"), a California corporation, and Warren E. Buffett and his wife beneficially owned approximately thirteen percent (13%) of that

* This percentage was computed without taking into account Mr. Buffett'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.

stock. On that date, Berkshire and its subsidiaries beneficially owned twenty-six percent (26%) 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. The Company takes up equity in earnings relating to its shareholdings in Blue Chip. For purposes of this Item 4, and pursuant to instruction no. 6 thereto, Blue Chip is deemed to be a subsidiary.

As of February 1, 1975, the Company, Associated and Columbia in the aggregate owned beneficially approximately eleven percent (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. Between February 3, 1975 and March 15, 1975, Associated purchased an additional 15,060 shares, representing approximately 1.5%, of the common stock of Berkshire. The Company takes up equity in earnings relating to its shareholdings in Berkshire. For purposes of this Item 4, and pursuant to instruction no. 6 thereto, Berkshire is deemed to be a subsidiary.

ITEM 5. PENDING LEGAL PROCEEDINGS.

Neither the Company, Associated nor Associated's subsidiaries are parties to any material pending legal proceedings other than ordinary routine litigation incidental to their business, and none of their property is the subject thereof.

The premises on which Associated operated two of its retail stores in Philadelphia, Pennsylvania, one of which was owned by Associated, and the other of which was leased by Associated, have been the subject of condemnation proceedings. Associated received

$1,348,095 and $134,809.50, in May, 1973 and December, 1974, respectively, as compensation for the store it owned. Associated's occupancy of the two stores terminated during April, 1974 and June, 1974. (See, ITEM 1. BUSINESS and ITEM 3. PROPERTIES.)

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	280

ITEM 8. EXECUTIVE OFFICERS OF THE REGISTRANT.

Name	Age (a)	Office(s) held
Warren E. Buffett	44	Chairman of the Board of Directors
Robert H. Goldman (b)	58	President; Director
David S. Gottesman	48	Vice-President; Director
Charles T. Munger	51	Vice-President; Director
Charles F. Heider	48	Director
Max E. Blumenthal (b)	34	Secretary
Larry C. Cummings (b)	31	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

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(a) The information is given as of February 1, 1975.

(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.

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.

ITEM 10. FINANCIAL STATEMENTS AND EXHIBITS FILED.

A. Financial statements

A list of the consolidated financial statements and schedules of the Company, and/or of the consolidated insurance 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 Berkshire Hathaway Inc.

Exhibit C: 1975 Annual Report of Blue Chip Stamps

Exhibit D: 1974 Annual Report of Wesco Financial Corporation

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 Farnam Street Omaha, Nebraska 68131	common	record and beneficial	437,089 (b)	43.70%
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 90014	common	record and beneficial	100,000 (d)	10.00%

(a) The information is given as of February 1, 1975.

(b) This amount includes the following shares of common stock, as to which Mr. Buffett disclaims the beneficial ownership:

(i) 32,065 shares held by members 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) 368 shares held in equal amounts in two 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) 1,536 shares held in two 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 10,643 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 47,061 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%

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 1, 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. Since 1970,

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(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 1, 1975.

(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 (Ambec, Columbia and Fashion Outlet).

(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 10,643 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.

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.

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 (b)

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 since the beginning of the fiscal year ended February 1, 1975, 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:*

(a) Subject to the exceptions indicated in note (b) 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 1, 1975.

(b) This amount does not include legal fees and cash advanced in the amounts of $18,834.00 and $133.45, respectively, which the Company accrued during its fiscal year ended February 1, 1975, 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, 1975, and February 1, 1975, for which amounts the said firm had not billed the Company as of February 1, 1975. (See ITEM 15. INTEREST OF MANAGEMENT AND OTHERS IN CERTAIN TRANSACTIONS.)

* 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.

(1) During the Company's fiscal year ended February 1, 1975, 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 $2,100,000. See Note 10 to Columbia's financial statements presented elsewhere. National Indemnity performs all of Columbia's bookkeeping and other administrative functions. For these services Columbia pays to National Indemnity as part of its ceding commissions an amount ordinarily equal to one half of the customary originating brokerage commissions. "Pro rata" business normally carried an originating commission of 1%, and "excess" business, an originating commission of 10%. The amount of ceding commissions representing fees for bookkeeping and administrative services paid by Columbia to National Indemnity during 1974 was approximately $21,943.

(2) During the Company's fiscal year ended February 1, 1975, the Company paid and/or incurred certain legal fees in connection with the representation of the Company by the law firm of Frank, Bernstein, Conaway & Goldman. (See note (b) to <u>ITEM 13. REMUNERATION OF DIRECTORS AND OFFICERS</u>.)

B. During the Company's fiscal year ended February 1, 1975, 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 1, 1975, there was 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 2, 1975

ANNUAL REPORT ON FORM 10-K

ITEM 10(a)

FINANCIAL STATEMENTS AND SCHEDULES

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

The following consolidated financial statements and schedules of the registrant and its subsidiaries and of the registrant (parent company) for the fiscal years 1975 and 1974 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". Schedules related to the insurance operations included in the consolidated financial statements have been filed only as a part of the financial statements and schedules of that consolidated insurance subsidiary included herein.

The following financial statements and schedules of the consolidated insurance subsidiary for the years 1974 and 1973 are submitted herewith:

- Consolidated Balance Sheet
- Consolidated Statement of Earnings
- Consolidated Statement of Capital Stock and Surplus
- Consolidated Statement of Changes in Financial Position
- Notes to Consolidated Financial Statements

Schedule I - Summary of Investments in Securities
Schedule II - Stocks - Other Than Stocks of Affiliates
Schedule III - 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 are omitted because the information required therein is not applicable or is given in the financial statements or notes thereto.

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

Exhibit A - Computation of Earnings Per Share
Exhibit B - Annual Report of Berkshire Hathaway Inc. - December 28, 1974
Exhibit C - Annual Report of Blue Chip Stamps - March 1, 1975
Exhibit D - Annual Report of Wesco Financial Corporation

ERNST & ERNST
ONE NORTH CHARLES
BALTIMORE, MARYLAND
21201

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

We have examined the balance sheet of Diversified Retailing Company, Inc. (parent company) as of February 1, 1975, and February 2, 1974, and the related statements of earnings, retained earnings and changes in financial position for the years then ended and the consolidated balance sheet of Diversified Retailing Company, Inc. and subsidiaries as of February 1, 1975, and February 2, 1974, and the related consolidated statements of earnings, retained earnings and changes in financial position for the years then ended 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 certain affiliated companies. The financial statements of these companies used as the basis of recording such equity in earnings and those of the consolidated insurance subsidiary were examined by other auditors whose reports were furnished to us. The consolidated financial statements of Columbia Insurance Company, the insurance subsidiary, reflect total assets and net earnings constituting 36% and 15% in 1975 and 34% and 31% in 1974, respectively, of the related consolidated totals. Our opinion expressed herein, insofar as it relates to the amounts included for the consolidated insurance subsidiary and to the amount of income included for those affiliated companies for each of the years ended February 1, 1975, and February 2, 1974, 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 10 to the financial statements of Blue Chip, which statements are included as Exhibit C to this annual report on Form 10-K. The investment in Blue Chip is carried at cost plus equity in undistributed earnings, which at February 1, 1975 aggregated $13,249,000.

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 financial statements referred to above present fairly the financial position of Diversified Retailing Company, Inc. (parent company) and the consolidated financial position of Diversified Retailing Company, Inc. and subsidiaries at February 1, 1975, and February 2, 1974, and the respective results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis, after restatement for the changes, with which we concur, in the method of accounting for the investment in the insurance subsidiary as described in Note A to the consolidated financial statements, and in the terms used to express changes in financial position from working capital to cash as shown in both the parent company and consolidated financial statements. Further, it is our opinion that Schedules III (subject to the effect of the aforementioned legal proceedings), V, VI and XVI referred to above present fairly the information set forth therein in compliance with the applicable accounting regulations of the Securities and Exchange Commission.

ERNST & ERNST

Baltimore, Maryland
April 28, 1975

CONSOLIDATED BALANCE SHEET

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

ASSETS

	February 1, 1975	February 2, 1974 (as restated)
Cash	$ 4,462,878	$ 2,517,666
U. S. Treasury bills - at cost, which approximates market	1,806,004	662,589
Accounts receivable - Note B	901,630	839,353
Merchandise inventories - Note A	4,220,012	4,313,442
Property and equipment - at cost less allowance for depreciation and amortization (1975 - $507,070; 1974 - $645,525) - Notes A and C	925,198	921,594
Investments, other than investments in affiliated companies - Notes A, D and E:		
Bonds, at amortized cost	1,788,450	1,038,971
Common stocks, at cost less a valuation allowance for anticipated losses of $300,000 at February 1, 1975	1,221,755	1,391,572
	3,010,205	2,430,543
Investments in affiliated companies - Notes A, D, F and G:		
Berkshire Hathaway Inc.	10,184,776	9,405,391
Blue Chip Stamps	13,249,060	12,490,857
	23,433,836	21,896,248
Other assets - Note A	709,156	602,306
	$39,468,919	$34,183,741

CONSOLIDATED BALANCE SHEET - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

LIABILITIES AND STOCKHOLDERS' EQUITY

	February 1, 1975	February 2, 1974 (as restated)
LIABILITIES		
Losses and loss adjustment expenses of consolidated insurance subsidiaries - Note A	$ 3,730,000	$ 1,921,122
Unearned insurance premiums of consolidated insurance subsidiaries - Note A	1,224,835	902,893
Accounts payable and accrued expenses, other than income taxes	2,491,307	1,172,760
Income taxes - Notes A and I:		
Current	419,304	418,652
Deferred	522,129	471,115
	941,433	889,767
8% Debentures due 1985 - Note H	6,600,000	6,600,000
9% Notes payable - Note H	1,239,154	1,242,885
Other liabilities	496,404	551,565
TOTAL LIABILITIES	16,723,133	13,280,992
STOCKHOLDERS' EQUITY - Notes H and J		
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	16,745,786	14,902,749
	22,745,786	20,902,749
COMMITMENTS AND CONTINGENT LIABILITIES - Notes K and L		
	$39,468,919	$34,183,741

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974 (as restated)
Net sales (including leased department sales)	$34,924,966	$38,398,636
Cost of goods sold	21,828,566	25,023,201
Gross profit	13,096,400	13,375,435
Insurance underwriting gain (loss)	(374,221)	67,743
Interest and dividend income	414,000	230,751
Other income	196,519	229,946
	13,332,698	13,903,875
Selling, general and administrative expenses	11,946,426	12,167,203
Interest and financing costs	676,758	720,066
	12,623,184	12,887,269
EARNINGS BEFORE INCOME TAXES, EQUITY IN EARNINGS OF AFFILIATED COMPANIES, REALIZED SECURITIES GAINS (LOSSES) AND EXTRAORDINARY ITEM	709,514	1,016,606
Applicable income taxes - Notes A and I	306,796	440,907
EARNINGS BEFORE EQUITY IN EARNINGS OF AFFILIATED COMPANIES, REALIZED SECURITIES GAINS (LOSSES) AND EXTRAORDINARY ITEM	402,718	575,699
Equity in earnings of affiliated companies - Notes A, F and G:		
Berkshire Hathaway Inc.	722,671	1,220,030
Blue Chip Stamps	859,011	765,275
	1,581,682	1,985,305
EARNINGS BEFORE REALIZED SECURITIES GAINS (LOSSES) AND EXTRAORDINARY ITEM	1,984,400	2,561,004
Realized gains (losses) on sales of securities, net of taxes (credit): 1975 - ($89,894); 1974 - $11,000	(209,754)	25,672
EARNINGS BEFORE EXTRAORDINARY ITEM	1,774,646	2,586,676
Extraordinary item - Note M	68,391	395,578
NET EARNINGS	$ 1,843,037	$ 2,982,254
Earnings per share:		
Earnings before equity in earnings of affiliated companies, realized securities gains (losses) and extraordinary item	$ .40	$ .58
Equity in earnings of affiliated companies	1.58	1.99
Realized securities gains (losses)	(.21)	.02
Extraordinary item	.07	.39
Net earnings	$ 1.84	$ 2.98

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974 (as restated)
Balance at beginning of year	$14,902,749	$11,920,495
Net earnings for the year	1,843,037	2,982,254
BALANCE AT END OF YEAR	$16,745,786	$14,902,749

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974 (as restated)
SOURCE OF FUNDS		
From operations:		
Net earnings before extraordinary item	$1,774,646	$2,586,676
Charges (credits) to earnings not affecting funds:		
Equity in current earnings of affiliated companies, net of deferred taxes	(1,581,682)	(1,985,305)
Dividends received from affiliated companies, net of current taxes	187,506	187,508
Increase in unpaid losses and loss adjustment expenses of insurance subsidiaries	1,124,859	679,672
Increase in unearned insurance premiums	158,409	57,634
Increase in accounts payable and accrued expenses	1,315,345	218,563
Depreciation and amortization of fixed assets	125,659	145,531
Provision for anticipated losses on common stocks, net of $90,000 deferred tax benefit	210,000	
Decrease (increase) in inventories	93,430	(494,922)
Decrease (increase) in receivable	(20,489)	(270,997)
Increase (decrease) in income taxes currently payable	(1,148)	64,079
Increase (decrease) in other liabilities	60,446	39,913
Amortization of excess of carrying amounts of net assets of consolidated subsidiaries over acquisition costs	(106,875)	(131,130)
All other	2,611	209,019
TOTAL FROM OPERATIONS, EXCLUDING EXTRAORDINARY ITEM	3,342,717	1,306,241
Extraordinary item	68,391	395,578
TOTAL FROM OPERATIONS	3,411,108	1,701,819
Proceeds from condemnation of property less gain included above		874,326
Sale of common stock	30,286	962,513
Decrease in short-term commercial paper		1,495,297
	$3,441,394	$5,033,955
APPLICATION OF FUNDS		
Investment in Berkshire Hathaway Inc.		$1,631,657
Purchase of insurance subsidiary - Note A	$ 497,800	
Other investments:		
Bonds	191,055	74,160
Common stocks	15,000	959,774
Additions to property, plant and equipment, net	129,263	185,111
Debt repayment	3,731	
Increase in treasury bills	1,143,415	563,873
Increase in cash	1,461,130	1,619,380
	$3,441,394	$5,033,955

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

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") and Columbia Insurance Company ("Columbia"), wholly-owned by Associated. This presentation differs from that used in previous financial statements issued by the Company, in which Associated's investment in Columbia was carried on the equity basis. Because of the nature of the insurance assets and liabilities now consolidated, the accompanying balance sheet no longer distinguishes between current and noncurrent assets and liabilities.

Intercompany accounts and transactions have been eliminated in consolidation.

Investment in Consolidated Subsidiaries

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 of $295,055 at February 1, 1975 and $426,185 at February 2, 1974 is included in other liabilities in the balance sheet.

Columbia was formed in 1970 by Associated. As of April 30, 1974, Columbia purchased 99.6% of the outstanding stock of Southern Casualty Insurance Company ("Southern"). Accounts of Southern since date of purchase by Columbia are included in consolidation. The cash purchase price for Southern was $497,800, including $72,555 excess of cost over net assets acquired. The excess cost is being amortized over approximately three years; the unamortized balance of $48,300 at February 1, 1975 is included in other assets in the balance sheet.

The financial statements of Southern at the acquisition date are summarized as follows:

ASSETS		LIABILITIES	
Cash	$ 484,082	Unpaid losses and loss adjustment expenses	$684,019
Bonds	558,424	Unearned premiums	163,533
Common stock	145,469	Other liabilities	20,525
Premiums and other receivables	41,788		$868,077
Other assets	63,559		
	$1,293,322		

Columbia and Southern maintain their records on a calendar-year basis in accordance with state insurance regulations, and calendar-year results and year-end balances of Columbia and Southern are included in Diversified's fiscal periods ending one month thereafter.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note A - Merchandise Inventories

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

Property and Equipment

Property and equipment represents that of the retailing subsidiaries. Expenditures for maintenance, repairs, renewals and betterments which represent improvements 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.

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.

Investments, other than investments in Affiliated Companies

These investments represent those of insurance subsidiaries.

Investments in bonds are stated at amortized cost. The aggregate market value of the bonds has not been determined but, at February 1, 1975, would be less than cost. No provision has been made for possible losses on bonds since the subsidiaries generally intend to hold bonds to maturity and do not expect to realize any significant losses upon their disposition.

Investments in common stocks are stated at cost less, at February 1, 1975, a valuation allowance for anticipated losses.

Investment in Affiliated Companies

The Company and its subsidiaries hold common stock investments in Berkshire Hathaway Inc. ("Berkshire") and Blue Chip Stamps ("Blue Chip"), 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 the equity 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, 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 that fiscal year.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note A - (Cont'd) This change had 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 operations of Blue Chip to which the excess cost originally related.

Blue Chip's 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 1, 1975, and February 2, 1974, the Company, Associated and Columbia held in the aggregate approximately 11% of the outstanding shares of Berkshire. In addition Warren E. Buffett, Chairman of the Board of both the Company and Berkshire and his wife, owned 36% of Berkshire's shares. Merging of the Company into Berkshire was proposed in early 1974; the proposal was abandoned by action of the Directors of both companies on January 28, 1975.

At February 1, 1975 and February 2, 1974, Associated and Columbia held approximately 16% of Blue Chip's outstanding shares. Warren E. Buffett and his wife owned 13% of Blue Chip's shares at both dates. Berkshire, at February 1, 1975, owned approximately 26% and, at February 2, 1974, approximately 19% of the outstanding shares of Blue Chip.

Financial statements of Berkshire, Blue Chip and, additionally, Wesco Financial Corporation - a 64%-owned subsidiary of Blue Chip - are included elsewhere herein.

Financing Costs

Certain costs incurred in connection with the issuance by the Company of its 8% Debentures have been capitalized and are being ratably amortized over the stipulated life of the debentures. Unamortized financing costs included in other assets at February 1, 1975 and February 2, 1974 were $302,868 and $331,071, respectively.

Losses and Loss Adjustment Expenses of Consolidated Insurance Subsidiaries

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. The insurance subsidiaries do not provide for estimated catastrophe losses.

Note A - (Cont'd) Insurance Premiums

Insurance premiums are recognized as earned ratably over the terms of the policies. Unearned premiums are computed on a monthly pro-rata basis. Policy acquisition costs or commissions are deferred and charged against income ratably over the terms of the policies for purposes of determining consolidated results of the Company and its subsidiaries.

Federal Income Taxes

The Company and its subsidiaries file a consolidated Federal income tax return. Insurance subsidiaries account for certain items of income and expense differently for financial reporting purposes than for income tax reporting purposes. Provisions are made for deferred taxes in recognition of these timing differences.

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).

Note B - ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following:

	February 1, 1975	February 2, 1974
Layaway accounts and other receivables of retailing operations	$258,528	$420,159
Uncollected premiums, net of commissions payable, of insurance operations	581,865	389,289
Reinsurance recoverable on loss payments	26,241	-
Investment income due and accrued	34,996	29,905
	$901,630	$839,353

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note C - PROPERTY AND EQUIPMENT

Property and equipment are comprised of the following:

	February 1, 1975	February 2, 1974
Land	$ 231,715	$ 201,515
Buildings	239,997	210,197
Building improvements	183,538	156,095
Leasehold improvements	194,312	352,913
Furniture, fixtures and equipment	582,706	646,399
	1,432,268	1,567,119
Less allowances for depreciation and amortization	507,070	645,525
	$ 925,198	$ 921,594

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.

Note D - SECURITIES DEPOSITED WITH OTHERS

Insurance subsidiaries deposited the following in trust with regulatory authorities or with ceding reinsurers in accordance with reinsurance treaties:

	December 31, 1974	December 31, 1973
Bonds, at amortized cost	$1,065,551	$ 895,769
Stocks, including those of affiliates, at cost	2,041,042	1,522,682

Note E - INVESTMENTS IN COMMON STOCKS OF UNAFFILIATED COMPANIES

The quoted market value of common stocks of unaffiliated companies was $849,700 at December 31, 1974 and $890,884 at December 31, 1973. At December 31, 1974, Columbia recognized as a realized loss a $300,000 provision for estimated losses on common stocks of unaffiliated companies. The difference of $372,055 between the remaining adjusted carrying value for such investments at December 31, 1974 and quoted market value is considered by management to be attributable to temporary market fluctuations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note F - INVESTMENT IN BERKSHIRE HATHAWAY INC.

The carrying value of the investment in 109,551 shares of 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 1, 1975	February 2, 1974
Purchase cost:		
Representing underlying net asset values at dates of acquisition	$ 6,299,017	$6,299,017
Cumulative excess of cost over equity in net assets at dates of acquisition, less amortization	328,061	336,350
	6,627,078	6,635,367
Equity in post-acquisition earnings	3,557,698	2,770,024
CARRYING AMOUNT	$10,184,776	$9,405,391

No dividends have been received from Berkshire. Equity in earnings of Berkshire shown in the statement of earnings represents the following:

	Year ended February 1, 1975	Year ended February 2, 1974
Equity in Berkshire's reported net earnings	$787,672	$1,320,353
Provision for deferred income taxes	(56,712)	(94,105)
Amortization of difference between cost and equity in net assets at dates of acquisition	(8,289)	(6,218)
	$722,671	$1,220,030

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note G - INVESTMENT IN BLUE CHIP STAMPS

The carrying value of the investment in 841,900 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:

	February 1, 1975	February 2, 1974
Purchase cost:		
Representing underlying net assets values at dates of acquisition	$ 6,988,300	$ 6,988,300
Cumulative excess of cost over equity in net assets at dates of acquisition less amortization	2,228,571	2,674,285
	9,216,871	9,662,585
Equity in post-acquisition undistributed earnings	4,032,189	2,828,272
CARRYING AMOUNT	$13,249,060	$12,490,857

Dividends from Blue Chip Stamps were $202,056 in each of the fiscal years ended February 1, 1975 and February 2, 1974. Equity in earnings of Blue Chip shown in the statements of earnings represents the following:

	Years ended February 1, 1975	Years ended February 2, 1974
Equity in Blue Chip's reported net earnings	$1,405,973	$1,304,945
Provision for income taxes, including deferred income taxes of $86,700, 1975 and $79,408, 1974	(101,248)	(93,956)
Amortization of excess of cost over equity in net assets at dates of acquisition	(445,714)	(445,714)
	$ 859,011	$ 765,275

Financial statements of Blue Chip appear elsewhere herein, and 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

Note G - (Cont'd) 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 it to discontinue issuance of trading stamps. However, the Company now considers forced consummation of any sale or spin-off unlikely.

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 class-action complaint against the Company 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. The class-action complaint was also amended effective September 19, 1974 to assert, in substance, that the Company's predecessor had engaged in similar conduct from 1961 until its merger into the Company in 1968, and that the Company must respond in respect of the alleged liability of its predecessor to plaintiffs and the persons they purport to represent for over-reimbursement of sales taxes. 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 as amended is estimated at $17,000,000 less the amount of any money which may be recovered on the claims against the state. Counsel believes the prospects for some 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.

Note G - (Cont'd) 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 stockholders. On petition of the Company, the United States Supreme Court granted review and on March 24, 1975 the case was argued and submitted for decision to the Supreme Court. On June 5, 1974 the Company was served with a complaint in a substantially identical action filed in Los Angeles County Superior Court on June 21, 1971. Further proceedings have been held in abeyance in this state action by mutual consent until determination by the United States Supreme Court in the federal 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."

Note H - 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 two years ended February 1, 1975, although the line was used for brief periods on a few occasions during the year ended February 2, 1974.

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

Note H - (Cont'd) 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 104.5% of par plus accrued interest to October 31, 1975 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.

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 $975,000 were subject to such restrictions at February 1, 1975.

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note H - 9% Notes Payable
(Cont'd)

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, 1975 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:

1976	$ 3,731
1977	109,731
1978 through 1981	3,731
1982	357,969
1983	571,299
1986 and 1987	26,500
1988	128,500

Note I - INCOME TAXES

The Company's consolidated federal income tax returns have been examined by the Internal Revenue Service through February 1, 1969.

Total income tax expense for the years ended February 1, 1975 and February 2, 1974 is summarized as follows:

	Year ended	
	February 1, 1975	February 2, 1974
INCOME TAXES APPLICABLE TO:		
Operating earnings	$306,796	$440,907
Equity in earnings of Berkshire Hathaway Inc.	56,712	94,105
Equity in earnings of Blue Chip Stamps	101,248	93,956
Realized gain (loss) on sales of securities	(89,894)	11,000
Extraordinary gain	36,000	213,000
TOTAL INCOME TAX EXPENSE	$410,862	$852,968
The above figures represent:		
State and local income taxes	$174,000	$197,000
Federal income taxes	236,862	655,968
	$410,862	$852,968

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note I - (Cont'd) Federal income taxes computed at the statutory 48% rate applied to income before taxes are reconciled to the Federal income tax expense figures reflected above as follows:

	Year ended February 1, 1975	Year ended February 2, 1974
Federal income taxes at statutory rate	$1,082,000	$1,842,000
Tax differences relating to:		
Dividends received credits, including credits applied to equity in earnings of Berkshire Hathaway Inc. and Blue Chip Stamps	(918,000)	(1,098,000)
Amortization of differences between cost and underlying net assets of subsidiaries and investees (not deductible for tax purposes)	167,000	154,000
Capital gain or loss rate differential	31,000	(116,000)
Federal tax benefit of state and local taxes	(84,000)	(86,000)
Tax exempt interest income	(39,000)	(30,000)
All other	(2,138)	(10,032)
	$ 236,862	$ 655,968

Note J - STOCKHOLDERS' EQUITY

There were no changes in the capital stock and additional paid-in capital accounts during the two years ended February 1, 1975 and February 2, 1974.

At February 1, 1975 retained earnings included $7,044,356 representing undistributed earnings of affiliated companies (net of income tax provisions) as follows: Berkshire Hathaway - $3,302,503; Blue Chip - $3,741,853.

Note K - LEASES

Associated and its retailing subsidiaries lease 67 stores, warehouse facilities and New York Offices, under leases expiring at various dates through 1988. The leases require minimum annual rentals plus, under the terms of certain leases, additional payments for taxes, other expenses and percentage rentals. Total rental expense on such facilities for the fiscal years ended February 1, 1975 and February 2, 1974 was approximately $1,788,000 and $1,844,000, respectively, including contingent rentals of approximately $213,000 and $229,000, respectively.

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note K - (Cont'd) Associated also has leased and leases data processing equipment for approximately $56,000 a year through the end of 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 the existing real estate leases were as follows at February 1, 1975:

Fiscal Year Ending 1976	$1,374,000
Fiscal Year Ending 1977	1,263,000
Fiscal Year Ending 1978	976,000
Fiscal Year Ending 1979	625,000
Fiscal Year Ending 1980	571,000
Fiscal Years Ending 1981-1985	1,831,000
Fiscal Years Ending 1986-1988	208,000
TOTAL	$6,848,000

Note L - PENSION PLAN

Associated has a noncontributory trusteed pension plan covering eligible full-time employees. The total pension expense for the fiscal years ended February 1, 1975 and February 2, 1974 was $73,000 and $63,000, respectively, 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 1, 1975 was approximately $100,000.

In the opinion of Associated's management, the effect on its pension costs of the Pension Reform Act of 1974 will not be substantial.

Note M - EXTRAORDINARY ITEMS

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. It

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

February 1, 1975 and February 2, 1974

Note M - (Cont'd) was estimated that an additional $135,000 would be realized from this proceeding; the latter amount was recognized in computing gain of $395,578 net of $213,000 income taxes, reflected as an extraordinary item in the statement of earnings for the year ended February 2, 1974. Proceeds over and above the $135,000 estimated as of February 2, 1974 were received in connection with those properties in the current fiscal year, and an additional gain of $68,391, net of $35,000 income taxes, is reflected as an extraordinary item in the statement of earnings for the year ended February 1, 1975.

Note N - SUPPLEMENTAL NOTE - INVENTORIES

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

February 3, 1973	$3,818,520
February 2, 1974	4,313,442
February 1, 1975	4,220,012

BALANCE SHEET

DIVERSIFIED RETAILING COMPANY, INC.

	February 1, 1975	February 2, 1974
ASSETS		
Cash	$ 7,336	$ 75,304
Note receivable from subsidiary	6,600,000	6,600,000
Investment in subsidiary - Notes A and B	22,025,026	20,394,648
Investment in affiliated company - Notes A and C	2,250,819	2,057,356
Unamortized cost of long-term financing - Note A	302,868	331,071
	$31,186,049	$29,458,379
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accrued interest and other expenses	$ 180,691	$ 179,703
Due to subsidiary	50,959	46,115
Deferred income taxes - Note A	74,404	60,742
8% Debentures - Note D	6,600,000	6,600,000
9% Notes payable - Note D	1,239,154	1,242,885
Unamortized excess of carrying amount of net assets of subsidiary over acquisition cost - Note A	295,055	426,185
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	16,745,786	14,902,749
	22,745,786	20,902,749
	$31,186,049	$29,458,379

See notes to financial statements.

STATEMENT OF EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974
Income:		
Interest from subsidiary	$ 528,000	$ 487,385
Amortization of excess of net assets of subsidiary over acquisition cost - Note A	131,130	131,130
	659,130	618,515
Expenses:		
General and administrative expenses	55,618	34,837
Interest and financing costs - Note A	667,810	668,146
	723,428	702,983
LOSS BEFORE INCOME TAXES, EQUITIES IN EARNINGS OF SUBSIDIARY AND AFFILIATED COMPANY	(64,298)	(84,468)
Federal income tax credit - Note A	97,156	103,500
INCOME BEFORE EQUITIES IN EARNINGS OF SUBSIDIARY AND AFFILIATED COMPANY	32,858	19,032
Equity in earnings of subsidiary - Notes A and B	1,630,378	2,637,388
Equity in earnings of affiliated company net of deferred income taxes: 1975 - $13,662; 1974 - $23,990 - Notes A and C	179,801	325,834
NET EARNINGS	$1,843,037	$2,982,254
Earnings per share:		
Income before equities in earnings of subsidiary and affiliated company	$ .03	$ .02
Equity in earnings of subsidiary	1.63	2.64
Equity in earnings of affiliated company	.18	.32
Net earnings	$ 1.84	$ 2.98

See notes to financial statements.

STATEMENT OF RETAINED EARNINGS

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974
Balance at beginning of year	$14,902,749	$11,920,495
Net earnings for the year	1,843,037	2,982,254
BALANCE AT END OF YEAR	$16,745,786	$14,902,749

See notes to financial statements.

STATEMENT OF CHANGES IN FINANCIAL POSITION

DIVERSIFIED RETAILING COMPANY, INC.

	Fiscal year ended February 1, 1975	Fiscal year ended February 2, 1974
SOURCE OF FUNDS		
From operations:		
Net earnings for the year	$1,843,037	$2,982,254
Charges (credits) to earnings which did not affect cash:		
Increase in accrued expenses	988	8,093
Amortization of excess of carrying amounts of net assets of subsidiary over acquisition cost	(131,130)	(131,130)
Amortization of long-term financing costs	28,203	28,202
Equity in earnings of subsidiary	(1,630,378)	(2,637,388)
Equity in earnings of Berkshire Hathaway Inc.	(179,801)	(325,834)
TOTAL FROM OPERATIONS	(69,081)	(75,803)
Net advances from subsidiary	4,844	67,115
Dividend from subsidiary		6,600,000
	(64,237)	6,591,312
APPLICATION OF FUNDS		
Loan to subsidiary		6,600,000
Debt repayment	3,731	
	3,731	6,600,000
DECREASE IN CASH	($ 67,968)	($ 8,688)

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

DIVERSIFIED RETAILING COMPANY, INC.

February 1, 1975 and February 2, 1974

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

The Company and its subsidiaries hold common stock investments in Berkshire Hathaway Inc. ("Berkshire") and Blue Chip Stamps ("Blue Chip"), which two companies are considered "investees" under the provisions of Accounting Principles Board Opinion No. 18. Accordingly, the Company and its subsidiaries use the equity method of accounting for these investments. Under the equity method, the Company currently recognizes its proportionate share of earnings reported by these 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 over a forty-year period of the difference between cost of the investments in Berkshire (the Company has no direct holdings in Blue Chip) and the underlying equity in net assets at the dates of acquisition.

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, has resulted in tax credits to Diversified.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

February 1, 1975 and February 2, 1974

Note B - INVESTMENT IN SUBSIDIARY

Associated holds common stock of Berkshire Hathaway Inc. and Blue Chip Stamps (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 1, 1975	Fiscal year ended February 2, 1974
Earnings before equity in earnings of unconsolidated subsidiary and affiliated companies and extraordinary gain	$ 444,851	$ 463,616
Equity in earnings of unconsolidated insurance subsidiary	268,779	912,811
Equity in earnings of affiliated companies	848,357	865,383
Extraordinary gain	68,391	395,578
NET EARNINGS	$1,630,378	$2,637,388

Associated's balance sheet at February 1, 1975 reflected total assets of $31,421,000, including $8,698,000 investment in its unconsolidated insurance subsidiary, $3,408,000 investment in Berkshire Hathaway Inc. and $9,377,000 investment in Blue Chip Stamps. Comparable figures at February 2, 1974 were: total assets $28,673,000; investment in unconsolidated insurance subsidiary, $8,429,000; investment in Berkshire Hathaway Inc., $3,170,000 and investment in Blue Chip Stamps, $8,821,000.

Note C - INVESTMENT IN AFFILIATED COMPANIES

At February 1, 1975 the Company, Associated and Columbia held 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 39% and 36%, respectively, of the outstanding common stock of these companies. A merger of the Company into Berkshire was proposed in early 1974. This proposal was abandoned by action of the directors of both companies on January 28, 1975.

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, the unamortized balance of which was $129,881 at February 1, 1975. Berkshire has paid no dividends during the period of the Company's affiliation.

Note C - (Cont'd) Financial statements of Berkshire, Blue Chip and, additionally, Wesco Financial Corporation, a 64%-owned subsidiary of Blue Chip, are included elsewhere herein. See also Note G to consolidated 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 104.5% of par plus accrued interest to October 31, 1975 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

Note D - (Cont'd) 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 $975,000 were subject to such restrictions at February 1, 1975.

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, 1975 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:

1976	$ 3,731
1977	109,731
1978 through 1981	3,731
1982	357,969
1983	571,299
1986 and 1987	26,500
1988	128,500

Note E - INCOME TAXES

The Company's consolidated federal income tax returns have been examined by the Internal Revenue Service through February 1, 1969.

Note F - STOCKHOLDERS' EQUITY

There were no changes in the capital stock and additional paid-in capital accounts during the fiscal years ended February 1, 1975 and February 2, 1974.

At February 1, 1975 retained earnings included $4,439,000 representing undistributed earnings of subsidiary and affiliated company as follows: Associated - $3,467,000 and Berkshire Hathaway - $972,000.

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SCHEDULE III - INVESTMENTS IN SECURITIES OR AFFILIATES

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

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 1, 1975:									
Affiliates:									
Blue Chip Stamps Common Stock	841,900	$12,490,857	$ 960,259		$202,056		841,900	$13,249,060	
Berkshire Hathaway Inc. Common Stock	109,551	9,405,391	779,385				109,551	10,184,776	
		$21,896,248	$1,739,644(1)		$202,056			$23,433,836	

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SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES - CONTINUED

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

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:									
Affiliates:									
Blue Chip Stamps Common Stock	841,900	$11,833,682	$ 859,231		$202,056		841,900	$12,490,857	
Berkshire Hathaway Inc. Common Stock	90,381	6,459,597	1,314,135	$1,631,659(2)			109,551	9,405,391	
		$18,293,279	$2,173,366	$1,631,659	$202,056			$21,896,248	

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SCHEDULE III - INVESTMENTS IN SECURITIES OF AFFILIATES

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 1, 1975:									
Associated Retail Stores, Inc.	453,000	$20,394,648	$1,630,378				453,000	$22,025,026	
Affiliate:									
Berkshire Hathaway Inc. Common Stock	26,392	$ 2,057,355	$ 193,463				26,392	$ 2,250,818	

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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	

	Consolidated 1975	Consolidated 1974	Parent Company 1975	Parent Company 1974
(1) Reconciliation to statement of earnings:				
Equity in earnings	$1,739,644	$2,173,366	$193,463	$349,824
Applicable income taxes	157,962	188,061	13,662	23,990
	$1,581,682	$1,985,305	$179,801	$325,834

(2) Acquisition of 19,091 and 80 shares, respectively, at cost by Associated and Columbia.

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 SUBSIDIARIES

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	Balance at Close of Period
				(A)	
Fiscal year ended February 1, 1975:					
Land	$ 201,515	$ 30,200			$ 231,715
Buildings	210,197	29,800			239,997
Building improvements	156,095	27,443			183,538
Leasehold improvements	352,913	6,434		($165,035)	194,312
Furniture, fixtures and equipment	646,399	37,300	$ 8,594	(92,399)	582,706
	$1,567,119	$131,177	$ 8,594	($257,434)	$1,432,268
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

(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 SUBSIDIARIES

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 (A)	Balance at End of Period
Fiscal year ended February 1, 1975:					
Buildings	$ 45,851	$ 11,308			$ 57,159
Building improvements	35,213	9,578			44,791
Leasehold improvements	225,087	27,452		($165,035)	87,504
Furniture, fixtures and equipment	339,374	77,321	$ 6,680	(92,399)	317,616
	$645,525	$125,659	$ 6,680	($257,434)	$507,070
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

(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.

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

SCHEDULE XVI—SUPPLEMENTARY INCOME STATEMENT INFORMATION

DIVERSIFIED RETAILING COMPANY, INC.

AND SUBSIDIARIES

COL. A	COL. B
ITEM	Charged to Costs and Expenses
Fiscal year ended February 1, 1975:	
Maintenance and repairs	$ 452,812
Depreciation and amortization of property, plant and equipment	125,659
Amortization of intangible assets	156
Taxes, other than income taxes:	
Payroll taxes	485,893
Personal property and real estate	200,959
Other	141,461
Rents:	
Real estate	1,787,789
Equipment	85,099
Royalties	None
Advertising	62,131
Research and development	None
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	156
Taxes, other than income taxes:	
Payroll taxes	479,545
Personal property and real estate	179,483
Other	232,559*
Rents:	
Real estate	1,843,817
Equipment	68,059
Royalties	None
Advertising	102,414
Research and development	None

* Other taxes for the year ended February 2, 1974 include $70,000 representing settlement with the states of New York and Pennsylvania for previously disputed gross receipts taxes applicable to several prior years.

COLUMBIA INSURANCE COMPANY

Financial Information for Inclusion in Annual 10-K Report

December 31, 1973 and 1974

PEAT, MARWICK, MITCHELL & CO.

CERTIFIED PUBLIC ACCOUNTANTS

ACCOUNTANTS' REPORT

The Board of Directors
Columbia Insurance Company:

We have examined the consolidated financial statements and related schedules of Columbia Insurance Company and consolidated subsidiary 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, $3,670,302 and $3,871,969 at December 31, 1973 and 1974, respectively, and $203,767 and $231,647 in equity in net earnings of other companies for 1973 and 1974, 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 1, 1975 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 8 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 consolidated financial statements present fairly the financial position of Columbia Insurance Company and consolidated subsidiary at December 31, 1973 and 1974 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, and the supporting schedules, as listed in the accompanying index, in our opinion, subject to the effect, if any, of the matters disclosed in the preceding paragraph related to the investment in Blue Chip Stamps included in Schedules III and X, present fairly the information set forth therein.

PEAT, MARWICK, MITCHELL & CO.

Peat, Marwick, Mitchell & Co.

Omaha, Nebraska
March 21, 1975

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Index to Consolidated Financial Statements

All other schedules are omitted because the information required therein is not applicable or is given in the financial statements or the notes thereto.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Consolidated Balance Sheets

December 31, 1973 and 1974

Assets	1973	1974
Cash	$ 13,608	124,828
Investments (note 3):		
U. S. Treasury Bills, at cost which approximates market	662,589	1,806,004
Bonds, at amortized value	1,038,971	1,788,450
Common stocks of unaffiliated companies - market 1973, $890,884; 1974, $849,700 (note 4)	1,391,572	1,221,755
Common stock of Berkshire Hathaway Inc. (note 5)	4,178,367	4,525,465
Common stock of Blue Chip Stamps (note 6)	3,670,302	3,871,969
Total investments	10,941,801	13,213,643
Uncollected premiums (net of commissions payable of $89,872, 1973; $151,499, 1974)	389,289	581,865
Reinsurance recoverable on loss payments	-	26,241
Investment income due and accrued	29,905	34,996
Recoverable Federal income taxes	-	42,844
Prepaid acquisition costs	142,000	133,000
Excess of cost over net assets of subsidiary purchased, net of accumulated amortization of $24,255	-	48,300
Other assets	186	72,662
	$ 11,516,789	14,278,379

Liabilities, Capital Stock and Surplus	1973	1974
Losses and claims	$ 1,493,040	3,031,633
Loss adjustment expenses	167,471	382,955
Unearned premiums	902,893	1,224,835
Assumed losses payable	260,661	315,412
Ceded reinsurance balances payable	-	163,418
Amounts retained by company for account of others	-	220,118
Income taxes (note 9):		
Current	29,522	-
Deferred	223,882	182,403
Total income taxes	253,404	182,403
Other liabilities	10,315	59,771
Total liabilities	3,087,734	5,580,545
Capital stock and surplus:		
Capital stock par value $100. Authorized, issued and outstanding, December 31, 1973 and 1974 - 20,000 shares (note 7)	2,000,000	2,000,000
Surplus:		
Paid-in	3,855,389	3,855,389
Unassigned	2,573,666	2,842,445
Total surplus	6,429,055	6,697,834
Total capital stock and surplus	8,429,055	8,697,834
	$ 11,516,789	14,278,379

See accompanying notes to consolidated financial statements.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Consolidated Statements of Earnings

Years ended December 31, 1973 and 1974

	1973	1974
Underwriting income:		
Net premiums written	$ 2,161,947	3,175,412
Increase in unearned premiums	57,634	321,942
Premiums earned	2,104,313	2,853,470
Losses incurred	1,367,098	2,139,325
Loss expense incurred	89,164	315,222
	1,456,262	2,454,547
	648,051	398,923
Underwriting expenses incurred:		
Commissions and brokerage	528,148	652,490
Taxes, licenses and fees	31,124	47,457
Other underwriting expenses	20,036	64,197
Decrease in prepaid acquisition costs	1,000	9,000
	580,308	773,144
Gain (loss) from underwriting	67,743	(374,221)
Investment income:		
Interest on bonds	99,083	191,864
Dividends, unaffiliated companies	58,078	56,762
	157,161	248,626
Investment expenses	1,840	28,444
Net investment income	155,321	220,182
Earnings (loss) before income taxes, equity in net earnings of other companies and realized investment losses	223,064	(154,039)
Income taxes (benefit) (note 9):		
Current	48,087	(76,648)
Deferred	1,000	(2,400)
	49,087	(79,048)
Earnings (loss) before equity in net earnings of other companies and realized investment losses	173,977	(74,991)
Equity in net earnings of other companies:		
Berkshire Hathaway Inc. (note 5)	590,321	321,877
Blue Chip Stamps (note 6)	203,767	231,647
	794,088	553,524
Earnings before realized investment losses	968,065	478,533
Investment losses - excludes unrealized appreciation (depreciation) in common stocks of unaffiliated companies of ($472,521) in 1973 and $128,623 in 1974:		
Realized investment losses (note 4)	(78,934)	(299,648)
Applicable income tax (benefit)	(23,680)	(89,894)
Net realized investment losses	(55,254)	(209,754)
Net earnings	$ 912,811	268,779

See accompanying notes to consolidated financial statements.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Consolidated Statements of Capital Stock and Surplus

Years ended December 31, 1973 and 1974

	Capital stock	Surplus Paid-in	Surplus Unassigned
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 (note 7)	1,500,000	(1,500,000)	-
Balance, December 31, 1973	2,000,000	3,855,389	2,573,666
Net earnings for the year	-	-	268,779
Balance, December 31, 1974	$ 2,000,000	3,855,389	2,842,445

See accompanying notes to consolidated financial statements.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Consolidated Statements of Changes in Financial Position

Years ended December 31, 1973 and 1974

	1973	1974
Funds provided:		
From operations:		
Net earnings	$ 912,811	268,779
Charges (credits) to earnings not requiring (providing) funds:		
Accretion of bond discount	(5,324)	(5,330)
Increase in estimated losses and loss expenses	483,799	1,070,058
Increase in unearned premiums	57,634	321,942
Increase in assumed losses payable	195,873	54,801
Increase (decrease) in deferred taxes	1,000	(92,400)
Increase in recoverable income taxes	-	(42,844)
Increase in accrued taxes and expenses	37,465	19,934
Increase in uncollected premiums	(116,551)	(158,877)
Decrease in accrued investment income	16,501	1,370
Decrease in prepaid acquisition costs	1,000	9,000
Loss (gain) on sale of investments	78,934	(352)
Provision for anticipated losses on common stocks	-	300,000
Equity in undistributed earnings of affiliated companies, net of deferred taxes	(738,408)	(497,844)
Amortization	159	24,411
Increase in ceded balances payable	-	160,216
Increase in reinsurance recoverable on loss payment	-	(26,241)
Funds provided from operations	924,893	1,406,623
From sale of common stocks of unaffiliated companies	676,816	30,638
Decrease in cash	2,658	372,862
Other, net	-	31,817
Total funds provided	$ 1,604,367	1,841,940
Funds used:		
Subsidiary acquired:		
Securities	-	703,893
Cash	-	484,082
Other assets	-	105,347
Excess of cost over net assets acquired	-	72,555
Estimated loss and loss adjustment expenses	-	(684,019)
Other liabilities	-	(184,058)
	-	497,800
Cost of investments purchased:		
Bonds	74,160	185,725
Common stocks:		
Unaffiliated companies	959,774	15,000
Affiliates	6,560	-
	1,040,494	200,725
Increase in U. S. Treasury Bills	563,873	1,143,415
Total funds used	$ 1,604,367	1,841,940

See accompanying notes to financial statements.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 1973 and 1974

(1) Summary of Significant Accounting Policies and Practices

(a) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its 99.6% owned subsidiary, Southern Casualty Insurance Company. The subsidiary was acquired April 30, 1974 (see note 2) and since such acquisition was accounted for as a purchase, the results of operations for the subsidiary are included in the consolidated statements of earnings only for the period subsequent to the date of acquisition. The excess of cost over the underlying net assets at the date of acquisition is being amortized over approximately three years using the straight-line method. All significant intercompany accounts and transactions have been eliminated in consolidation.

(b) Investment in Securities, Other Than Affiliates

Investments in bonds are stated at cost, adjusted where appropriate for amortization of premium or accretion of discount. The aggregate market value of bonds has not been determined but such market value would be less than amortized cost. No provision has been made for possible losses on such bonds since the companies intend to hold the bonds to maturity and do not expect to realize any significant losses.

Investments in common stocks are stated at cost less a valuation allowance for anticipated losses.

(c) Investment 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 January 1, 1973. This change has the effect of reducing income for the year ended December 31, 1973 by $126,000. 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.

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.

(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. Policy acquisition costs or commissions are deferred and charged against income ratably over the terms of the policies.

(e) 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.

(f) Catastrophe Losses

The Company does not provide an estimate for catastrophe losses. The Financial Accounting Standards Board, 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.

(Continued)

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Notes to Consolidated Financial Statements, Continued

(g) 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 companies join Associated Retail Stores, Inc., the parent of Columbia Insurance Company, in filing consolidated income tax returns.

(2) Acquisition

The Company purchased Southern Casualty Insurance Company (Southern Casualty) on April 30, 1974 for a cash purchase price of $497,800. Southern Casualty is licensed to write workmen's compensation insurance in the State of Louisiana. Had the purchase of Southern Casualty been consummated as of January 1, 1973 consolidated premiums earned and earnings on a pro forma basis would have been:

	Year ended December 31 (unaudited)	
	1973	1974
Premiums earned	$ 3,108,921	2,916,243
Earnings (loss) before equity in net earnings of other companies and realized investment losses	188,026	(109,444)
Equity in net earnings of other companies	794,088	553,524
Realized investment losses, net	(75,990)	(204,408)
Net earnings	$ 906,124	239,672

(3) Securities Deposited with Others

Certain bonds and stocks deposited in trust with regulatory authorities or with ceding reinsurers in accordance with various reinsurance treaties were as follows:

	1973	1974
Bonds, at amortized cost	$ 895,769	1,065,551
Stocks, cost	1,522,682	2,041,042
	$ 2,418,451	3,106,593

(4) Common Stocks of Unaffiliated Companies

The Company recognized a $300,000 provision for anticipated losses on common stocks of unaffiliated companies as a realized investment loss in 1974. Accordingly, the investment in such stocks is reported at cost less the allowance for anticipated losses. The investments in common stocks of unaffiliated companies and the related market values are as follows:

	1973	1974
Cost	$ 1,391,572	1,521,755
Allowance for anticipated losses	-	300,000
	$ 1,391,572	1,221,755
Approximate market value	$ 890,884	849,700

(Continued)

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Notes to Consolidated Financial Statements, Continued

(5) 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, 1973	December 31, 1974
Shares owned	48,715	48,715
Percentage of total outstanding shares (approximate)	5%	5%
Cost represented by:		
Underlying net asset values at dates of acquisition	$ 2,668,740	2,668,740
Excess cost, net of amortization of $4,241 at December 31, 1973 and $7,406 at December 31, 1974	123,528	120,363
	2,792,268	2,789,103
Equity in post-acquisition earnings	1,386,099	1,736,362
Carrying value	$ 4,178,367	4,525,465

Deferred income taxes of approximately $100,000 at December 31, 1973 and $125,000 at December 31, 1974 have been provided with respect to the equity in post-acquisition earnings, assuming their ultimate distribution as a taxable dividend.

(6) 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, 1973	December 31, 1974
Cost represented by:		
Underlying net asset values at dates of acquisition	$ 1,912,829	1,912,829
Excess cost, net of amortization of $195,645 at December 31, 1973 and $351,478 at December 31, 1974	992,401	836,568
	2,905,230	2,749,397
Equity in post-acquisition undistributed earnings	765,072	1,122,572
Carrying value	$ 3,670,302	3,871,969

Through December 31, 1972, the excess cost over underlying net asset values was being written off over a forty year period. Commencing with 1973, this period of amortization was reduced to seven years (see note 1).

Deferred income taxes of approximately $55,000 at December 31, 1973 and $81,000 at December 31, 1974 have been provided with respect to the equity in post-acquisition undistributed earnings, assuming their ultimate distribution as a taxable dividend.

(Continued)

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Notes to Consolidated Financial Statements, Continued

(7) 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.

(8) 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 it to discontinue issuance of trading stamps. However, the Company now considers forced consummation of any sale or spin-off unlikely.

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 class-action complaint against the Company 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. The class-action complaint was also amended effective September 19, 1974 to assert, in substance, that the Company's predecessor had engaged in similar conduct from 1961 until its merger into the Company in 1968, and that the Company must respond in respect of the alleged liability of its predecessor to plaintiffs and the persons they purport to represent for overreimbursement of sales taxes. 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 as amended is estimated at $17,000,000 less the amount of any money which may be recovered on the claims against the state. Counsel believes the prospects for some 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)

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 stockholders. On petition of the Company, the United States Supreme Court granted review and on March 24, 1975 the case was argued and submitted for decision to the Supreme Court. On June 5, 1974 the Company was served with a complaint in a substantially identical action filed in Los Angeles County Superior Court on June 21, 1971. Further proceedings have been held in abeyance in this state action by mutual consent until determination by the United States Supreme Court in the Federal 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."

(9) Income Taxes

Income tax expense (benefit) is made up of the following:

	1973	1974
Totals:		
Expense (benefit) applicable to operating earnings	$ 49,087	(79,048)
Expense applicable to equity in earnings of:		
Berkshire Hathaway Inc.	46,046	25,220
Blue Chip Stamps	27,900	30,021
Benefit applicable to investment losses	(23,680)	(89,894)
	$ 99,353	(113,701)
Income tax currently payable (recoverable) relating to:		
Earnings (loss) before Federal income taxes, equity in net earnings of other companies and realized investment gain (loss)	48,087	(76,648)
Distributed earnings of Blue Chip Stamps	4,320	4,320
Realized investment gain (loss)	(23,680)	106
Total current carried forward	$ 28,727	(72,222)

(Continued)

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Notes to Consolidated Financial Statements, Continued

	1973	1974
Total current brought forward	$ 28,727	(72,222)
Deferred expense (credit) relating to:		
Equity in undistributed earnings of other companies:		
Berkshire Hathaway Inc.	46,046	25,220
Blue Chip Stamps	23,580	25,701
Accreted discount on bonds	1,500	1,900
Credit for tax effect of reduction in deferred acquisition costs	(500)	(4,300)
Provision for anticipated loss on sale of investment securities	-	(90,000)
Total deferred	70,626	(41,479)
Total income tax expense (credit)	$ 99,353	(113,701)

Total net income after taking into account realized investment losses but before income taxes was $1,012,164 in 1973 and $155,078 in 1974. Income tax expense of $485,839 in 1973 and $74,437 in 1974 would result if computed by applying the statutory U. S. Federal income tax rate of 48% to income before taxes. The differences are reconciled as follows:

	1973	1974
Tax expense at statutory rate	$ 485,839	74,437
Increase (reduction) in income taxes resulting from:		
Tax-exempt interest	(30,576)	(39,138)
85% dividends received credit relating to:		
Dividends received from unaffiliated companies	(23,696)	(23,159)
Equity in net earnings of other companies	(419,030)	(313,247)
Amortization of cost in excess of the underlying equity in net assets of affiliated companies and subsidiary	76,321	87,961
Capital loss rate differential	14,208	53,937
Tax benefit to parent in consolidation	-	43,481
Other	(3,713)	2,027
Total income tax expense (benefit)	$ 99,353	(113,701)

(10) Transactions with Affiliates

The Company derives the major portion of its business through the assumption of reinsurance contracts from insurance subsidiaries of Berkshire Hathaway Inc. The amounts included in the financial statements relating to such transactions are as follows:

	December 31,	
	1973	1974
Earned premiums	$ 1,449,510	1,839,304
Unearned premiums	630,311	919,958
Incurred losses and loss adjustment expenses	1,103,675	1,433,643
Commissions	406,543	554,626

Schedule I

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Summary of Investments in Securities - Other than Securities of Affiliates

December 31, 1974

Type of Security	Cost* and carrying value	Market value**	Admitted asset value
Bonds:			
States, municipalities and political subdivisions	$ 1,531,752	1,514,264	1,531,752
Industrial and miscellaneous	256,698	230,744	256,698
Total bonds	1,788,450	1,745,008	1,788,450
Common stocks:			
Public utilities	290,131	272,253	272,253
Banks, trusts and insurance companies	126,067	136,025	136,025
Industrial and miscellaneous	1,105,557	441,422	441,422
Total common stocks	1,521,755	849,700	849,700
Allowance for anticipated losses	300,000	-	-
Net common stocks	1,221,755	849,700	849,700
U. S. Treasury Bills	1,806,004	1,806,004	1,806,004
Total investments in securities - other than securities of affiliates	$ 4,816,209	4,400,712	4,444,154

*Cost represents original cost of stocks, and, as to debt obligations, original cost adjusted for amortization of premiums or accretion of discount.

**"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.

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Stocks - Other than Stocks of Affiliates

December 31, 1974

Name of issuer and title of issue	Number of shares	Cost and book value	Market and admitted asset value
Public utilities:			
California Water Service Co.	11,062	$ 275,449	259,957
Eastern Gas & Fuel	515	14,682	12,296
		290,131	272,253
Banks, trusts and insurance companies:			
National Detroit Corporation	100	5,113	2,925
New England Merchants Co., Inc.	100	2,313	1,100
Omaha National Corporation	8,800	118,641	132,000
		126,067	136,025
Industrial and miscellaneous:			
CIT Financial	200	8,210	6,175
Continental Corporation	400	18,158	13,600
Dresser Industries	300	14,936	13,125
Dun & Bradstreet	200	7,010	3,850
General Electric	100	6,325	3,337
Heinz, H. J., Co.	200	9,385	7,650
IBM	100	28,421	16,800
Morse Shoe, Inc.	20,000	153,100	45,000
Munsingwear, Inc.	5,000	90,722	57,500
Post Corporation	5,200	55,900	27,300
Knight (Ridder) Newspapers	300	14,986	4,350
Koppers Co.	100	4,266	3,750
Santa Fe International	300	8,685	7,012
Sunstrand	200	5,419	2,450
Tenneco	200	4,986	4,700
United Southern Agency	24	15,000	8,823
Vornado, Inc.	57,600	660,048	216,000
		1,105,557	441,422
Total common stocks		1,521,755	849,700
Allowance for anticipated losses		300,000	-
Net investment in common stocks		$ 1,221,755	849,700

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Investments in Stocks of Affiliates

December 31, 1974

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	4,525,465	2,192,175	2,192,175
Blue Chip Stamps	250,000	3,100,875	3,871,969	1,312,500	1,312,500
	298,715	$ 5,897,386	8,397,434	3,504,675	3,504,675

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

Schedule III

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COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Premiums, Losses and Underwriting Expenses

Year ended December 31, 1973

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	$ 252,858	386,695	279,125	360,428	450,120			
Allied lines	59,907	56,465	2,590	113,782	(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	741,380	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	266	490			
Boiler and machinery	183	241	-	424	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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COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Premiums, Losses and Underwriting Expenses

Year ended December 31, 1974

	Part 1 - Premiums				Part 2 - Losses and underwriting expenses			
Line of insurance	Unearned premiums beginning of period	Net premiums written	Unearned premiums end of period	Premiums earned during period	Losses incurred during period	Loss expense incurred during period	Commissions and brokerage incurred during period	Other under-writing expense incurred during period
Fire	$ 279,125	316,176	259,967	335,334	(62,474)			
Allied lines	2,590	77,543	63,602	16,531	45,753			
Homeowners multiple peril	138	309	136	311	-			
Commercial multiple peril	10,019	4,551	2,708	11,862	18,552			
Ocean marine	2,037	14,644	5,528	11,153	5,724			
Inland marine	10,738	23,622	12,119	22,241	114,316			
Earthquake	-	1,117	-	1,117	-			
Workmen's compensation	6,117	706,481	26,681	685,917	646,941			
Liability other than auto	166,296	275,011	225,844	215,463	183,514			
Auto liability	143,742	321,817	34,725	430,834	326,376			
Auto physical damage	13,131	50,459	21,106	42,484	38,456			
Aircraft (all perils)	2,200	52,026	18,714	35,512	27,756			
Surety	5,254	(6)	1,824	3,424	4,725			
Burglary and theft	224	650	-	874	14			
Boiler and machinery	-	-	-	-	280			
International	19,865	38,340	7,229	50,976	29,698			
Reinsurance	241,417	1,292,672	544,652	989,437	759,694			
	$ 902,893	3,175,412	1,224,835	2,853,470	2,139,325	315,222	652,490	111,654

Schedule VII

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Schedule X

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

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 X

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

Income from Dividends - Equity in Net Profit of Affiliates

Year ended December 31, 1974

Name of issuer and title of issue	Amount of cash dividends	Amount of equity in net profit
Public utilities:		
California Water Service	$ 22,566	-
Eastern Gas & Fuel	155	-
	22,721	-
Banks, trusts and insurance companies:		
Cleveland Trust Company	10	-
Girard Company	162	-
Harris Bank Corporation, Inc., Chicago	27	-
National Detroit Corporation	246	-
New England Merchants Co., Inc.	140	-
Omaha National Corporation	17,468	-
Pittsburgh National Corporation	39	-
State Street Boston Financial	30	-
Third National Corp., Nashville	50	-
	18,172	-
Industrial and miscellaneous:		
Berkshire Hathaway Inc.	-	321,877*
Boeing Corporation	15	-
Blue Chip Stamps	-	231,647*
CIT Financial	220	-
Continental Corporation	740	-
Dresser Industries	315	-
Dun & Bradstreet	144	-
General Electric	80	-
Grumann Corporation	30	-
Heinz, H. J., Co.	112	-
IBM	556	-
Investors Diversified Services	11	-
Knight (Ridder) Newspapers	48	-
Kennecott Copper Corporation	50	-
Koppers Co.	167	-
Morse Shoe, Inc.	4,000	-
Munsingwear, Inc.	5,400	-
Northrup Corporation	53	-
Post Corporation	3,536	-
Santa Fe International	67	-
Sunstrand	80	-
Tenneco	232	-
Washington Post Company	13	-
	15,869	553,524
	$ 56,762	553,524

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

Schedule XI

COLUMBIA INSURANCE COMPANY AND CONSOLIDATED SUBSIDIARY

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

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)

Year ended December 31, 1974

Type of security	Aggregate costs	Aggregate proceeds	Gain (loss)
Stocks:			
Banks, trust and insurance companies	$ 18,415	19,495	1,080
Industrial and miscellaneous	11,868	11,140	(728)
Provision for anticipated losses	-	-	(300,000)
	$ 30,283	30,635	(299,648)
Income tax benefit applicable to realized losses			89,894
Net realized losses			$(209,754)

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EXHIBIT A

COMPUTATION OF EARNINGS PER SHARE

	Fiscal year ended				
	February 1, 1975	February 2, 1974	February 3, 1973	January 29, 1972	January 30, 1971
Average shares outstanding	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Net earnings	$1,843,037 (5)	$2,982,254 (4)	$2,918,042 (2)	$1,515,880 (1)(3)	$1,720,265 (3)
Per share amount	$ 1.84	$ 2.98	$ 2.92	$ 1.52	$ 1.72

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

(2) Includes gain of $193,021 on sale of investments originally reported as extraordinary item. Shown in summary of operations as realized securities gain instead of extraordinary item.

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

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

(5) Includes extraordinary gain of $68,391.

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Berkshire Hathaway Inc.

1974

ANNUAL REPORT TO THE STOCKHOLDERS

Berkshire Hathaway Inc.

1974 Annual Report to the Stockholders

BUSINESS OF THE COMPANY

The Company is engaged in the manufacture and sale of woven textiles in the United States and through a subsidiary in the sale of textile products in Canada. Through subsidiaries collectively referred to in this annual report as the Insurance Group, the Company is engaged in the underwriting of fire and casualty insurance throughout the United States. The Company owns approximately 98% of The Illinois National Bank & Trust Co. of Rockford, Illinois which is engaged in the commercial banking business. The company and subsidiary members of the Insurance Group have significant holdings in Blue Chip Stamps, a California corporation — the businesses of which are more fully described herein.

CONTENTS

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Berkshire Hathaway Inc.

To the Stockholders of
Berkshire Hathaway Inc.:

Operating results for 1974 overall were unsatisfactory due to the poor performance of our insurance business. In last year's annual report some decline in profitability was predicted but the extent of this decline, which accelerated during the year, was a surprise. Operating earnings for 1974 were $8,383,576, or $8.56 per share, for a return on beginning shareholders' equity of 10.3%. This is the lowest return on equity realized since 1970. Our textile division and our bank both performed very well, turning in improved results against the already good figures of 1973. However, insurance underwriting, which has been mentioned in the last several annual reports as running at levels of unsustainable profitability, turned dramatically worse as the year progressed.

The outlook for 1975 is not encouraging. We undoubtedly will have sharply negative comparisons in our textile operation and probably a moderate decline in banking earnings. Insurance underwriting is a large question mark at this time – it certainly won't be a satisfactory year in this area, and could be an extremely poor one. Prospects are reasonably good for an improvement in both insurance investment income and our equity in earnings of Blue Chip Stamps. During this period we plan to continue to build financial strength and liquidity, preparing for the time when insurance rates become adequate and we can once again aggressively pursue opportunities for growth in this area.

Textile Operations

During the first nine months of 1974 textile demand was exceptionally strong, resulting in very firm prices. However, in the fourth quarter significant weaknesses began to appear, which have continued into 1975.

We currently are operating at about one-third of capacity. Obviously, at such levels operating losses must result. As shipments have fallen, we continuously have adjusted our level of operations downward so as to avoid building inventory.

Our products are largely in the curtain goods area. During a period of consumer uncertainty, curtains may well be high on the list of deferrable purchases. Very low levels of housing starts also serve to dampen demand. In addition, retailers have been pressing to cut inventories generally, and we probably are feeling some effect from these efforts. These negative trends should reverse in due course, and we are attempting to minimize losses until that time comes.

Insurance Underwriting

In the last few years we consistently have commented on the unusual profitability in insurance underwriting. This seemed certain eventually to attract unintelligent competition with consequent inadequate rates. It also has been apparent that many insurance organizations, major as well as minor, have been guilty of significant underreserving of losses, which inevitably produces faulty information as to the true cost of the product being sold. In 1974, these factors, along with a high rate of inflation, combined to produce a rapid erosion in underwriting results.

The costs of the product we deliver (auto repair, medical payments, compensation benefits, etc.) are increasing at a rate we estimate to be in the area of 1% per month. Of course, this increase doesn't proceed in an even flow but, inexorably, inflation grinds very heavily at the repair services – to humans and to property – that we provide. However, rates virtually have been unchanged in the property and casualty field for the last few years. With costs moving forward rapidly and prices remaining unchanged, it was not hard to predict what would happen to profit margins.

Best's, the authoritative voice of the insurance industry, estimates that in 1974 all auto insurance premiums in the United States increased only about 2%. Such a growth in the pool of dollars available to pay insured losses and expenses was woefully inadequate. Obviously, medical costs applicable to people injured during the year, jury awards for pain and suffering, and body shop charges for repairing damaged cars increased at a dramatically greater rate during the year. Since premiums represent the sales dollar and the latter items represent the cost of goods sold, profit margins turned sharply negative.

As this report is being written, such deterioration continues. Loss reserves for many giant companies still appear to be understated by significant amounts, which means that these competitors continue to underestimate their true costs. Not only must rates be increased sufficiently to match the month-by-month increase in cost levels, but the existing expense-revenue gap must be overcome. At this time it appears that insurors must experience even more devastating underwriting results before they take appropriate pricing action.

All major areas of insurance operations, except for the "home state" companies, experienced significantly poorer results for the year.

The direct business of National Indemnity Company, our largest area of insurance activity, produced an underwriting loss of approximately 4% after several years of high profitability. Volume increased somewhat, but we are not encouraging such increases until rates are more adequate. At some point in the cycle, after major insurance companies have had their fill of red ink, history indicates that we will experience an inflow of business at compensatory rates. This operation, headed by Phil Liesche, a most able underwriter, is staffed by highly profit-oriented people and we believe it will provide excellent earnings in most future years, as it has in the past.

Intense competition in the reinsurance business has produced major losses for practically every company operating in the area. We have been no exception. Our underwriting loss was something over 12% – a horrendous figure, but probably little different from the average of the industry. What is even more frightening is that, while about the usual number of insurance catastrophes occurred during 1974, there really was no "super disaster" which might have accounted for the poor figures of the industry. Rather, a condition of inadequate rates prevails, particularly in the casualty area where we have significant exposure. Our reinsurance department is run by George Young, an exceptionally competent and hard-working manager. He has cancelled a great many contracts where prices are totally inadequate, and is making no attempt to increase volume except in areas where premiums are commensurate with risk. Based upon present rate levels, it seems highly unlikely that the reinsurance industry generally, or we, specifically, will have a profitable year in 1975.

Our "home state" companies, under the leadership of John Ringwalt, made good progress in 1974. We appear to be developing a sound agency group, capable of producing business with acceptable loss ratios. Our expense ratios still are much too high, but will come down as the operation develops into units of economic size. The Texas problem which was commented upon in last year's report seems to be improving. We consider the "home state" operation one of our more promising areas for the future.

Our efforts to expand Home and Automobile Insurance Company into Florida proved disastrous. The underwriting loss from operations in that market will come to over $2 million, a very large portion of which was realized in 1974. We made the decision to drop out of the Florida market in the middle of 1974, but losses in substantial amounts have continued since that time because of the term nature of insurance contracts, as well as adverse development on outstanding claims. We can't blame external insurance industry conditions for this mistake. In retrospect, it is apparent that our management simply did not have the underwriting information and the pricing knowledge necessary to be operating in the area. In Cook County, where Home and Auto's volume traditionally has been concentrated, evidence also became quite clear during 1974 that rates were inadequate. Therefore, rates were increased during the middle of the year but competition did not follow; consequently, our volume has dropped significantly in this area as competitors take business from us at prices that we regard as totally unrealistic.

While the tone of this section is pessimistic as to 1974 and 1975, we consider the insurance business to be inherently attractive. Our overall return on capital employed in this area – even including the poor results of 1974 – remains high. We have made every effort to be realistic in the calculation of loss and expense reserves. Many of our competitors are in a substantially weakened financial position, and our strong capital picture leaves us prepared to grow significantly when conditions become right.

Insurance Investment Results

Investment funds generated from the operation of our insurance companies continued to grow during 1974. Investment income grew correspondingly, and produced overall profitability for the insurance group despite the poor underwriting results. As the insurance group balance sheet shows, we have increased liquidity substantially. This trend has continued since yearend. With poor underwriting and with generally weakened capital ratios throughout the insurance industry, such a higher level of liquidity is appropriate and comforting. It eliminates the possible temptation to write business at any price, simply to maintain cash flow, which is a major problem faced by many companies.

Several comments regarding market value of securities may be appropriate. Between the insurance group and the bank, we have approximately $140 million invested in bonds. About $20 million of this investment is in very short-term Treasury securities or commercial paper, neither of which is subject to other than negligible market fluctuation. This leaves about $120 million in bonds of longer maturities, with a very large percentage of this sum in municipal bonds with an average maturity of perhaps twelve to fifteen years. Because of our large liquid position and inherent operating characteristics of our financial businesses, it is quite unlikely that we will be required to sell any quantity of such bonds under disadvantageous conditions. Rather, it is our expectation that these bonds either will be held to maturity or sold at times believed to be advantageous.

However, on any given day the market value of our bond portfolio is determined by yields available on comparable securities. Such market values can swing dramatically. For example, during 1974 a leading index of high-grade municipals increased in yield from a level of 5.18% at the beginning of the year to 7.08% at the end of the year. In the bond market, each 1/100 of 1% change in yield is referred to as a "basis point" and thus, a change of 1% in interest levels is referred to as 100 basis points. As measured by the index, bond yields increased 190 basis points during 1974. On a fifteen-year bond, an increase of 10 basis points translates to about a 1% downward change in market value. On $120 million of such bonds, it is therefore clear that a change of 10 basis points in yields (which easily can happen in one day) changes the market value of our bond portfolio by something over $1 million. Thus, in 1974 our bond portfolio, which probably had a market value roughly approximating its carrying value at the start of the year, had a market value substantially below carrying value at the end of the year. The market value of our bond portfolio will continue to move in both directions in response to changes in the general level of yields but we do not consider such movements, and the unrealized gains and losses that they produce, to be of great importance as long as adequate liquidity is maintained.

Our stock portfolio declined again in 1974 – along with most equity portfolios – to the point that at yearend it was worth approximately $17 million less than its carrying value. Again, we are under no pressure to sell such securities except at times that we deem advantageous and it is our belief that, over a period of years, the overall portfolio will prove to be worth more than its cost. A net capital loss was realized in 1974, and very likely again will occur in 1975. However, we consider several of our major holdings to have great potential for significantly increased values in future years, and therefore feel quite comfortable with our stock portfolio. At this writing, market depreciation of the portfolio has been reduced by more than half from yearend figures, reflecting higher general stock market levels.

Banking Operations

There is little new to say about Illinois National Bank and Trust. With Eugene Abegg running the operation, the exceptional has become the commonplace. Year after year he continues to run one of the most profitable banks in the United States, while paying maximum interest rates to depositors, operating with unusual levels of liquidity, and maintaining a superior level of loan quality.

Two factors specifically should be noted in looking at the separate income statement of the bank. The effect of filing a consolidated tax return is reflected in their figures, with the tax loss of the insurance operations used to offset the tax liability created by banking operations. Also, a property tax formerly paid by the bank now is assessed to the parent company and is reflected in corporate selling and administrative expense. Because of accruals, this had a double effect at both the bank and corporate level in 1974.

Under present money market conditions, we expect bank earnings to be down somewhat in 1975 although we believe they still are likely to compare favorably with those of practically any banking institution in the country.

Blue Chip Stamps

During 1974 we increased our holdings of Blue Chip Stamps to approximately 25½% of the outstanding shares of that company. Overall, we are quite happy about the results of Blue Chip and its prospects for the future. Stamp sales continue at a greatly reduced level, but the Blue Chip management has done an excellent job of adjusting operating costs. The See's Candy Shops, Inc. subsidiary had an outstanding year, and has excellent prospects for the future.

Your Chairman is on the Board of Directors of Blue Chip Stamps, as well as Wesco Financial Corporation, a 64% owned subsidiary, and is Chairman of the Board of See's Candy Shops, Inc. We expect Blue Chip Stamps to be a source of continued substantial earning power for Berkshire Hathaway Inc.

The annual report of Blue Chip Stamps, which will contain financial statements for the year ended March 1, 1975 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.

Merger with Diversified Retailing Company, Inc.

As you previously have been informed, the proposed merger with Diversified Retailing Company, Inc. was terminated by the respective Boards of Directors on January 28, 1975. We continue to view such a merger as eventually desirable, and hope to reopen the subject at some future time.

Warren E. Buffett,
Chairman of the Board

March 31, 1975

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 28, 1974 and December 29, 1973, the statements of assets and liabilities of the Berkshire Hathaway Inc. - Insurance Group as of December 31, 1974 and 1973, 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 28, 1974 and December 29, 1973 and the statements of income and realized investment gains (losses), paid-in and unassigned surplus and changes in financial position of the Berkshire Hathaway Inc. - Insurance Group for the years ended December 31, 1974 and 1973. 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 2, 1974. Unaudited earnings of Blue Chip Stamps for the nine months ended November 30, 1974 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 $1,052,000 in earnings of Blue Chip Stamps for 1974.

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 28, 1974 and December 29, 1973 and the Berkshire Hathaway Inc. - Insurance Group at December 31, 1974 and 1973 and the results of their operations and the changes in their financial position for the respective years then ended in accordance with generally accepted accounting principles consistently applied during the period subsequent to the change, with which we concur, made as of January 1, 1973, in the method of determining inventory valuations, as described in note 7 to consolidated financial statements.

Peat, Marwick, Mitchell & Co.

March 14, 1975

Berkshire Hathaway Inc.
AND
CONSOLIDATED SUBSIDIARIES

Financial Statements
1974 and 1973

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

ASSETS	Dec. 28, 1974	Dec. 29, 1973
Cash	$ 4,230,559	$ 2,885,645
Investments:		
U. S. Treasury Bills and other short-term obligations, at cost which approximates market	11,108,163	1,400,435
Bonds, at amortized cost (notes 2 and 3)	71,530,651	73,074,026
Preferred stocks, at cost – market, 1974 – $1,842,817; 1973 – $2,186,960 (note 3)	2,855,185	2,298,348
Common stocks of unaffiliated companies, at cost – market, 1974 – $34,802,358; 1973 – $37,344,291 (note 3)	50,669,865	49,756,778
Common stock of Blue Chip Stamps (note 4)	16,923,998	13,717,274
Unconsolidated bank subsidiary (note 5)	22,416,879	21,003,034
Other unconsolidated subsidiaries (note 5)	1,187,333	1,333,832
Recoverable Federal income taxes	2,800,734	–
Accounts receivable from customers, agents and others, net (note 6)	17,891,227	14,056,574
Inventories (note 7)	5,999,552	7,136,676
Real estate, equipment, furniture and leasehold improvements, at cost less allowance for depreciation and amortization (note 8)	3,913,473	3,668,005
Deferred insurance premium acquisition costs	4,400,000	5,240,000
Other assets	285,954	560,987
	$216,213,573	$196,131,614

LIABILITIES AND STOCKHOLDERS' EQUITY		
Losses and loss adjustment expenses	$ 72,761,097	$ 61,675,768
Unearned premiums	21,704,867	21,281,980
Funds held under reinsurance treaties	2,857,284	1,318,205
Amounts due for purchase of securities	294,101	459,609
Accounts payable and accrued expenses	4,435,325	4,726,609
Income taxes:		
Current	163,809	262,357
Deferred	3,043,800	3,297,368
7½% debentures due 1987 (note 9)	555,780	598,540
8% promissory note due 1988 (note 10)	1,274,437	–
8% senior notes due 1993 (note 11)	20,000,000	20,000,000
Excess of net assets of consolidated subsidiaries over cost of investment	579,070	579,070
Other liabilities	345,376	776,642
	128,014,946	114,976,148
Stockholders' equity:		
Common stock of $5 par value. Authorized 1,100,000 shares; issued and outstanding, 979,569 shares	4,897,845	4,897,845
Retained earnings (note 11)	83,300,782	76,257,621
Total stockholders' equity	88,198,627	81,155,466
Commitment (note 13)		
	$216,213,573	$196,131,614

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

	52 weeks ended	
	Dec. 28, 1974	Dec. 29, 1973
Income items:		
Insurance premiums earned	$ 60,573,729	$ 52,929,257
Net sales of textile products	32,591,874	33,410,551
Interest and dividend income	8,029,876	7,378,109
Real estate income	286,307	287,017
	101,481,786	94,004,934
Cost and expense items:		
Insurance losses and loss adjustment expenses	47,119,846	32,835,798
Cost of textile products sold	27,429,277	28,305,725
Insurance underwriting expenses	20,345,744	16,774,167
Selling, administrative and other expenses	3,640,720	3,363,223
Interest expense	1,717,944	1,606,313
	100,253,531	82,885,226
Earnings from insurance underwriting and manufacturing operations before applicable income taxes	1,228,255	11,119,708
Income taxes (credit) applicable to operating earnings (note 12)	(2,010,321)	2,979,016
Earnings before equity in net earnings of other companies and realized investment gains (losses)	3,238,576	8,140,692
Equity in net earnings of bank subsidiary	4,093,000	2,781,900
Equity in net earnings of Blue Chip Stamps	1,052,000	1,008,000
Earnings before realized investment gains (losses)	8,383,576	11,930,592
Realized investment gains (losses)	(1,908,093)	1,331,550
Applicable income taxes (credit)	(567,678)	401,699
Net realized investment gains (losses)	(1,340,415)	929,851
In the absence of operating or investment reasons compelling liquidation, it is inappropriate to reflect in income temporary fluctuations in market values of long-term equity investments. Consequently, investment results exclude unrealized market decreases in investments in preferred and common stocks of unaffiliated companies of $4,356,000 in 1974 and $13,741,000 in 1973 (note 3).		
Net earnings	7,043,161	12,860,443
Retained earnings at beginning of year	76,257,621	64,024,663
Excess of cost over par value of treasury stock retired in 1973	–	(627,485)
Retained earnings at end of year	$ 83,300,782	$ 76,257,621
Earnings per share of common stock, based on 979,569 shares outstanding:		
Earnings before realized investment gains (losses)	$ 8.56	$12.18
Realized investment gains (losses)	(1.37)	.95
Net earnings	$ 7.19	$13.13

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

	52 weeks ended	
	Dec. 28, 1974	Dec. 29, 1973
Funds provided:		
From operations:		
Net earnings	$ 7,043,161	$ 12,860,443
Charges (credits) to earnings not requiring (providing) funds:		
Equity in undistributed earnings of bank subsidiary	(1,406,345)	(530,444)
Equity in undistributed earnings of Blue Chip Stamps	(889,410)	(900,000)
Accretion of discount on bonds	(442,153)	(481,767)
Depreciation and amortization	538,063	519,608
Increase in unpaid losses and loss expense	11,085,329	1,400,750
Increase (decrease) in unearned premiums	422,887	(2,557,417)
Increase in funds held under reinsurance treaties	1,539,079	360,360
Increase in accounts receivable from customers, agents and others	(3,834,653)	(1,202,693)
Decrease (increase) in inventories	1,137,124	(309,633)
Decrease in deferred insurance premium acquisition costs	840,000	384,000
Decrease in liability for income taxes	(352,116)	(3,230,468)
Increase in recoverable income taxes	(2,800,734)	–
Increase (decrease) in accounts payable and accrued expenses	(291,284)	342,851
Other, net	(329,243)	(27,860)
	5,216,544	(6,232,713)
Funds provided from operations	12,259,705	6,627,730
Dividends received from unconsolidated subsidiary	191,500	–
Proceeds from issuance of long-term debt	1,305,623	20,000,000
Decrease in cash	–	2,112,580
	$ 13,756,828	$ 28,740,310
Funds used:		
Net purchase (sale) of investments:		
U. S. Treasury Bills and other short-term obligations	9,707,728	(2,189,809)
Bonds	(1,985,528)	(11,965,977)
Preferred stocks	556,837	(643,904)
Common stocks of unaffiliated companies	913,087	32,344,998
Common stock of Blue Chip Stamps	2,317,313	1,529,878
Investment in unconsolidated subsidiary	45,000	75,000
	11,554,437	19,150,186
Additions to real estate, equipment, furniture and leasehold improvements	783,531	547,364
Repayment of long-term debt	72,946	9,042,760
Increase in cash	1,344,914	–
	$ 13,756,828	$ 28,740,310

See accompanying notes to consolidated financial statements.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 28, 1974 and December 29, 1973

(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. Certain 1973 amounts have been reclassified to conform with 1974 presentation.

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 less dividends received from such subsidiaries.

The accounts of the parent Company and its noninsurance 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 carried at cost. The aggregate market values of these investments, at both December 31, 1974 and December 31, 1973 were substantially less than their cost. The Company generally intends to hold the bonds to maturity and does not expect to realize significant losses from disposition of bonds. The investment in equity securities are held by the Insurance Group and generally consist of a relatively few issues acquired with a general view to holding as long-term investments. In view of the fact that market value quotations fluctuate daily, management considers the cost method as most appropriate for such long-term investments in the absence of operating reasons compelling their liquidation, and in the absence of evidence supporting a conclusion that their net cost will not eventually be recovered.

(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 on or about 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 insurers in the amount of $4,583,628 at December 31, 1974 and $3,281,480 at December 31, 1973. 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) Losses and Loss Adjustment Expenses

The Insurance Group provides 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 $5,518,385 at December 31, 1974 and $4,421,537 at December 31, 1973.

(f) Catastrophe Reserves

The Insurance Group does not provide a reserve for catastrophe losses. The Financial Accounting Standards Board 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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

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.

(h) Inventories

Inventories relate to the textile operation and are stated at cost determined under the last-in, first-out method.

(i) Income Taxes

A consolidated Federal income tax return is filed by the parent Company and its eligible subsidiaries. The recoverable amount or liability for current income taxes reflected in the consolidated balance sheets includes the apportioned Federal tax amounts of the companies whose accounts are consolidated.

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 $15,294,910 and $13,932,645 at December 31, 1974 and 1973, respectively, were deposited in trust with various regulatory authorities or others in accordance with the terms of certain reinsurance treaties.

(3) Investments in Securities of Unaffiliated Companies

A summary of the aggregate cost and approximate market value of investments in securities of unaffiliated companies at December 31, 1974 and 1973 is as follows:

	1974		1973	
	Cost	Market	Cost	Market
Bonds	$71,530,651	$58,907,900	$73,074,026	(a)

(a) The aggregate market value for the bond portfolio as of December 31, 1973 was not specifically determined. Management believed that the aggregate cost as of that date approximated market valuation.

	1974		1973	
	Cost	Market	Cost	Market
Preferred stocks ...	$ 2,855,185	$ 1,842,817	$ 2,298,348	$ 2,186,960
Common stocks ...	50,669,865	34,802,358	49,756,778	37,344,291
	$53,525,050	$36,645,175	$52,055,126	$39,531,251

The excess of cost over quoted market value of investments in preferred and common stocks of unaffiliated companies increased by $4,355,950 in 1974 and $13,741,037 in 1973, and aggregated $16,879,857 at December 31, 1974. While the timing and extent of a recovery in the market prices of these stocks cannot be predicted, management noted a recovery exceeding $10,000,000 in the quoted market value of its equity securities during the first ten weeks of 1975, and does not believe that the excess of cost over market value at December 31, 1974 represents a decline which justifies a write-down in carrying values.

In the first ten weeks of 1975, the Company realized losses of approximately $1,500,000, net of income tax credit applicable to such losses, from sales of securities. However, management believes that over the long term, no significant net loss to the Company will result from its continued holding or sale of the securities which constituted its portfolio at December 31, 1974.

(4) Investment in Blue Chip Stamps

The carrying value of the investment in Blue Chip Stamps ("Blue Chip") represents the cost, less amortization of the net excess of cost over equity in net assets at dates

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

of acquisition, plus equity in undistributed earnings. Deferred taxes of $191,800 and $100,000 at December 31, 1974 and 1973, respectively, 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:

	December 31, 1974	December 31, 1973
Shares owned	1,325,233	989,483
Percentage of total outstanding shares	25.6%	19%
Cost, represented by:		
Underlying net asset values at dates of acquisition	$13,084,112	$ 9,115,779
Net excess cost, less amortization of $1,179,873, 1974 and $795,673, 1973	870,603	2,905,822
	13,954,715	12,021,601
Equity in post-acquisition undistributed earnings	2,969,283	1,695,673
	$16,923,998	$13,717,274

The excess of cost over equity in net assets is being amortized over eight years from the beginning of 1972. Amortization was $384,200 for 1974 and $480,000 for 1973.

Blue Chip, a California corporation, is engaged primarily in the business of furnishing a trading stamps service to retail merchants and their customers in the states of California, Nevada and Oregon. A separate division of Blue Chip, on a nationwide basis, develops incentive programs for all types of businesses and also programs under which oil companies and other large issuers of credit cards can offer merchandise to their credit card holders. A subsidiary of Blue Chip, See's Candy Shops, Incorporated, manufactures candies in its kitchens located in Los Angeles and South San Francisco. The candies are sold through company-operated stores, approximately 170 in number, located in nine western states including Hawaii. Blue Chip also controls Mutual Savings and Loan Association through its ownership of approximately 64% of the outstanding capital stock of Wesco Financial Corporation, a registered savings and loan holding company. Mutual's head office is in Pasadena, California, and its approximately 15 other locations are in Southern California.

As indicated above, Berkshire Hathaway Inc. and its subsidiaries own approximately 26% of Blue Chip; these holdings plus holdings of other persons who may be considered affiliates aggregate over 50% of Blue Chip's outstanding shares.

The financial statements of Blue Chip as of March 2, 1974, and for the 52 weeks then ended (audited), and as of November 30, 1974 and for the 52 weeks then ended (unaudited) reflect the following:

BLUE CHIP STAMPS
Consolidated Balance Sheets

Assets	($000 omitted) *Mar. 2, 1974*	*Nov. 30, 1974 (Unaudited)*
Cash	$ 3,013	$ 3,322
Marketable securities, at cost (market March 2 — $128,654; November 30 — $73,040)	132,743	97,072
Inventories	10,355	16,083
Other current assets	8,913	14,140
Property, fixtures and equipment, net	10,453	8,736
Unamortized debenture discount	982	708
Investment in Wesco Financial Corporation	17,446	26,053
Excess of cost over equity in net assets of consolidated subsidiary	16,314	15,992
	$200,220	$182,106
Liabilities and Stockholders' Equity		
Liability for unredeemed trading stamps	$ 78,776	$ 71,705
Current portion of long-term debt	8,881	1,805
Other current liabilities	11,004	11,585
Note payable to bank, less current portion	33,000	27,200
6¾% subordinated debentures due 1978, less current portion	8,672	6,504
Stockholders' equity	59,887	63,307
	$200,220	$182,106

BLUE CHIP STAMPS
Consolidated Earnings Summaries

	($000 omitted) 52 weeks ended *Mar. 2, 1974*	52 weeks ended *Nov. 30, 1974 (Unaudited)*
Stamp service revenues	$ 51,375	$ 28,476
Incentive sales	6,261	9,620
Candy sales	35,780	39,259
Other revenues	8,803	9,747
Total revenues	$102,219	$ 87,102
Earnings before securities losses and extraordinary credit	8,190	8,035
Per share	1.58	1.55
Net earnings	8,005	7,178
Per share	1.55	1.39

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

Blue Chip financial statements for their fiscal year ended March 2, 1974 (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 2, 1974 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 13 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 $23,604,212 at December 28, 1974 and $22,336,866 at December 29, 1973 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) Receivables

Accounts receivable from customers, agents and others was made up of the following:

	December 31, 1974	December 31, 1973
Insurance Group:		
Agents' balances and premiums in course of collection	$ 9,583,769	$ 6,891,777
Investment income due and accrued	1,438,492	1,409,869
Reinsurance recoverable on loss payments	2,459,093	498,924
Amounts due from sale of securities	31,955	107,765
	13,513,309	8,908,335
Textile business trade accounts receivable (less allowance for doubtful accounts, 1974—$331,394; 1973—$332,679)	4,377,918	5,148,239
	$17,891,227	$14,056,574

(7) Inventories

A summary of inventories follows:

	Dec. 28, 1974	Dec. 29, 1973
Raw materials and supplies	$ 832,210	$ 1,047,827
Stock in process	1,425,670	1,604,824
Griege and finished cloth	3,741,672	4,484,025
	$ 5,999,552	$ 7,136,676

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 cost will generally be more nearly matched against current revenues in the statements of earnings and retained earnings. The change had the effect of reducing inventories at December 29, 1973 by $588,348 and net earnings by $294,174 ($0.30 per share) for the 52 weeks then ended.

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

The composition of plant and equipment is shown below:

December 28, 1974	*Properties of textile operations*	*Properties of Insurance Group*	*Total*
Land	$ 84,860	$ 83,847	$ 168,707
Buildings	2,409,214	1,254,363	3,663,577
Machinery and equipment	12,734,171	—	12,734,171
Furniture and fixtures and leasehold improvements	834,992	1,053,380	1,888,372
	16,063,237	2,391,590	18,454,827
Less accumulated depreciation and amortization	13,730,358	810,996	14,541,354
	$ 2,332,879	$1,580,594	$ 3,913,473
December 29, 1973			
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	663,325	14,007,895
	$ 2,062,833	$1,605,172	$ 3,668,005

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(9) 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, annually on August 1 to and including 1986.

(10) 8% Promissory Note Due 1988

The parent Company issued in May 1974 a promissory note in the principal amount of $1,305,623, repayable in monthly installments of $13,071 including interest at 8% per annum, through February 1988.

(11) 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 $25,000,000 as of December 28, 1974 and $21,000,000 as of December 29, 1973 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.

(12) Income Taxes

Net recoverable income taxes credited to 1974 earnings were made up as follows:

	U. S. Federal	*Foreign, state and local*	*Total*
Totals:			
(Credit) charge applicable to operating earnings	$(2,187,851)	$177,530	$(2,010,321)
Charge applicable to equity in earnings of Blue Chip Stamps	112,090	–	112,090
(Credit) applicable to realized investment losses	(567,678)	–	(567,678)
	$(2,643,439)	$177,530	$(2,465,909)
Currently (recoverable) payable:			
From net operating loss from insurance underwriting and manufacturing operations	(1,842,483)	177,530	(1,664,953)
On dividends from Blue Chip Stamps	20,290	–	20,290
From carryback of realized investment losses	(567,678)	–	(567,678)
Total current	(2,389,871)	177,530	(2,212,341)
Deferred expense (credit):			
On equity in undistributed earnings of Blue Chip Stamps	91,800	–	91,800
On net accreted discount on bonds	75,632	–	75,632
Credit for tax effect of reduction in deferred insurance premium acquisition costs	(421,000)	–	(421,000)
Total deferred	(253,568)	–	(253,568)
Total income tax credits	$(2,643,439)	$177,530	$(2,465,909)

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

Total net income in 1974 after taking into account realized investment losses, but before income taxes, was $4,577,252. Income tax expense of approximately $2,197,000 would result if computed by applying the statutory U. S. Federal income tax rate of 48% to income before taxes. A reconciliation of the difference is as follows:

	Amount
Tax expense at statutory rate	$ 2,197,000
Increases (decreases) resulting from:	
Tax-exempt interest income	(2,082,000)
100% exclusion relating to equity in earnings of The Illinois National Bank	(1,965,000)
85% dividends received credit:	
On dividends from unaffiliated companies	(1,065,000)
On equity in earnings of Blue Chip Stamps	(632,000)
Amortization of excess of cost over net assets of subsidiary and investee (not deductible for tax purposes)	230,000
Capital loss rate differential (30% vs. 48%)	343,000
Tax benefits to unconsolidated subsidiary	620,000
Miscellaneous	(111,909)
Net income tax credits	$(2,465,909)

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

	U. S. Federal	Foreign state and local	Total
Totals applicable to:			
Earnings from insurance underwriting and manufacturing operations	$2,764,952	$214,064	$2,979,016
Equity in earnings of Blue Chip Stamps	116,000	–	116,000
Realized investment gains	401,699	–	401,699
	$3,282,651	$214,064	$3,496,715
Current tax expense:			
On earnings from insurance underwriting and manufacturing operations	$2,781,668	$214,064	$2,995,732
On dividends from Blue Chip Stamps	16,000	–	16,000
On realized investment gains	401,699	–	401,699
Total current	3,199,367	214,064	3,413,431
Deferred tax expense (credit):			
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 deferred	83,284	–	83,284
Total income tax expense	$3,282,651	$214,064	$3,496,715

Total income tax expense of $3,496,715 is less than the amount of $7,851,000 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
Tax expense at statutory rate	$ 7,851,000
Increases (decreases) resulting from.	
Tax-exempt interest	(2,304,000)
100% exclusion relating to equity in earnings of The Illinois National Bank	(1,335,000)
85% dividends received credit:	
On dividends from unaffiliated companies	(542,000)
On equity in earnings of Blue Chip Stamps	(655,000)
Amortization of excess of cost over net assets of subsidiary and investee (not deductible for tax purposes)	290,000
Miscellaneous	191,715
Total income tax expense	$ 3,496,715

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

(13) "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.

(14) "Savings and Loan Holding Company" Status

The Company, as a result of its investment in Blue Chip Stamps which in turn holds controlling interest in a California 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.

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Berkshire Hathaway Inc.
INSURANCE GROUP

Financial Statements
1974 and 1973

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Berkshire Hathaway Inc.

INSURANCE GROUP

STATEMENTS OF ASSETS AND LIABILITIES

	December 31, 1974	December 31, 1973
ASSETS		
Bonds, at amortized cost (note 2)	$ 71,530,651	$ 73,074,026
Investments in stocks of unaffiliated companies, at cost:		
Preferred stocks (market, 1974 – $1,842,817; 1973 – $2,186,960)	2,855,185	2,298,348
Common stocks (market, 1974 – $34,802,358; 1973 – $37,344,291)	50,669,865	49,756,778
Total common and preferred stocks	53,525,050	52,055,126
U. S. Treasury Bills, at cost which approximates market	9,138,663	1,400,435
Investment in Blue Chip Stamps (note C)	14,370,980	13,717,274
Real estate, furniture and equipment (note 8)	1,580,594	1,605,172
Cash and bank deposits	1,513,636	1,465,359
Recoverable Federal income taxes	2,600,734	–
Agents' balances and premiums in course of collection	9,583,769	6,891,777
Reinsurance recoverable on loss payments	2,459,093	498,924
Investment income due and accrued	1,438,492	1,409,869
Amounts due from sale of securities	31,955	107,765
Other assets	164,605	373,525
Deferred acquisition costs	4,400,000	5,240,000
	$172,338,222	$157,839,252
LIABILITIES, CAPITAL STOCK AND SURPLUS		
Losses and loss adjustment expenses	$ 72,761,097	$ 61,675,768
Unearned premiums	21,704,867	21,281,980
Funds held under reinsurance treaties	2,857,284	1,318,205
Accrued expenses	1,328,944	916,341
Income taxes:		
Current	–	442,302
Deferred	3,034,000	3,297,368
Amounts due for purchase of securities	259,476	459,609
Other liabilities	161,654	745,361
	102,107,322	90,136,934
Capital stock and surplus (note D):		
Common stock of National Indemnity Company of $10 par value. Authorized 750,000 shares; issued 550,000 shares	5,500,000	5,500,000
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	20,601,250
Unassigned surplus (note 11)	41,629,650	39,101,068
Total capital stock and surplus	70,230,900	67,702,318
	$172,338,222	$157,839,252

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

STATEMENTS OF INCOME AND REALIZED INVESTMENT GAINS (LOSSES)

	Year ended December 31, 1974	1973
Underwriting income:		
Net premiums written	$ 60,996,616	$ 50,371,841
(Increase) decrease in unearned premiums	(422,887)	2,557,416
Premiums earned	60,573,729	52,929,257
Losses and loss expenses incurred	47,119,846	32,835,798
	13,453,883	20,093,459
Underwriting expenses:		
Commissions and brokerage	13,016,977	11,033,458
Salaries and other compensation	2,816,024	2,323,863
Taxes, licenses and fees	1,396,162	1,060,329
Other underwriting expenses	2,276,581	1,972,517
Decrease in deferred acquisition costs	840,000	384,000
	20,345,744	16,774,167
Net underwriting gain (loss)	(6,891,861)	3,319,292
Investment income:		
Interest on bonds	5,103,543	5,621,743
Dividends on stock (other than from Blue Chip Stamps)	2,811,980	1,688,024
Real estate income	286,307	287,017
	8,201,830	7,596,784
Investment expenses	322,010	313,894
Net investment income	7,879,820	7,282,890
Profit from underwriting and investments	987,959	10,602,182
Other expense	95,708	322,287
Income before income taxes, equity in earnings of Blue Chip Stamps and realized investment gains (losses)	892,251	10,279,895
Applicable income taxes (credit) (note E)	(2,184,761)	2,346,719
Income before equity in earnings of Blue Chip Stamps and realized investment gains (losses)	3,077,012	7,933,176
Equity in earnings of Blue Chip Stamps (note C)	791,985	1,008,000
Income before realized investment gains (losses)	3,868,997	8,941,176
Realized investment gains (losses)	(1,908,093)	1,331,550
Applicable income taxes (credit)	(567,678)	401,699
Net realized investment gains (losses)	(1,340,415)	929,851
Net income	$ 2,528,582	$ 9,871,027

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

STATEMENTS OF PAID-IN AND UNASSIGNED SURPLUS

	Year ended December 31, 1974	1973
PAID-IN SURPLUS		
Beginning of year	$ 20,601,250	$ 9,851,250
Contribution from parent	—	9,750,000
Excess of proceeds over par value of capital stock issued	—	1,000,000
End of year	$ 20,601,250	$ 20,601,250
UNASSIGNED SURPLUS		
Beginning of year	$ 39,101,068	$ 29,230,041
Net income	2,528,582	9,871,027
End of year	$ 41,629,650	$ 39,101,068

See accompanying notes to financial statements.

Berkshire Hathaway Inc.
INSURANCE GROUP

STATEMENTS OF CHANGES IN FINANCIAL POSITION

	Year ended December 31, 1974	Year ended December 31, 1973
Funds provided:		
From operations:		
Net income	$ 2,528,582	$ 9,871,027
Charges (credits) to income not requiring (providing) funds:		
Equity in undistributed earnings of Blue Chip Stamps	(653,706)	(900,000)
Accretion of discount on bonds	(442,153)	(481,767)
Depreciation	147,972	128,689
Increase in unpaid losses and loss expense	11,085,329	1,400,750
Increase (decrease) in unearned premiums	422,887	(2,557,417)
Increase in funds held under reinsurance treaties	1,539,079	360,360
Increase in agents' balances and premiums in course of collection	(2,691,992)	(511)
Increase in reinsurance recoverable on loss payments	(1,960,169	(221,183)
Decrease in deferred acquisition costs	840,000	384,000
Decrease in liability for income taxes	(705,670)	(2,615,563)
Increase in recoverable income taxes	(2,600,734)	—
Other, net	(115,130)	(62,460)
	4,865,713	(4,565,102)
Funds provided from operations	7,394,295	5,305,925
Additional capital paid in by shareholders	—	12,250,000
Decrease in cash	—	1,579,008
	$ 7,394,295	$ 19,134,933
Funds used:		
Net purchase (sale) of investments:		
U. S. Treasury Bills	7,738,228	(2,189,809)
Bonds	(1,965,528)	(11,965,977)
Preferred stocks	556,837	(643,904)
Common stocks of unaffiliated companies	913,087	32,344,998
Common stock of Blue Chip Stamps	—	1,529,878
	7,222,624	19,075,186
Purchase of real estate, furniture and equipment	123,394	59,747
Increase in cash	48,277	—
	$ 7,394,295	$ 19,134,933

See accompanying notes to financial statements.

Berkshire Hathaway Inc.

INSURANCE GROUP

NOTES TO FINANCIAL STATEMENTS

December 31, 1974 and 1973

(A) Note References

Numerical note references are to the notes to consolidated financial statements of Berkshire Hathaway Inc. and consolidated subsidiaries. Note 1 to such statements includes a summary of significant accounting policies and practices of the Insurance Group.

(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 (statutory methods) in accordance with which the companies maintain their records. A reconciliation of the aggregate capital stock and surplus ("Surplus as regards Policyholders") as determined under the statutory method to that determined and reported herewith in accordance with GAAP is as follows:

	December 31, 1974	December 31, 1973
Statutory surplus as regards Policyholders	$37,201,793	$41,595,522
Excess of cost over NAIC market valuations of investments in equity securities (excluding stock of Blue Chip Stamps)	16,449,675	12,523,925
Excess of carrying value of investment in Blue Chip Stamps (determined under GAAP pursuant to the equity method) over NAIC market valuation	9,176,194	6,545,772
Deferred insurance premium acquisition costs	4,400,000	5,240,000
Excess statutory liability loss reserves	1,850,644	1,469,116
Net recoverable from unauthorized reinsurers	1,788,012	1,483,393
Sundry nonadmitted assets	1,042,892	977,590
Income tax effects and adjustments	(1,678,310)	(2,133,000)
Capital stock and surplus — GAAP	$70,230,900	$67,702,318

Statutory net income is reconciled to GAAP net income as follows:

	1974	1973
Statutory net income	$2,354,072	$8,893,491
Decrease in deferred acquisition costs	(840,000)	(384,000)
Equity in undistributed earnings of Blue Chip Stamps, net of amortization of excess cost	653,706	900,000
Amortization of excess cost of investment in Home and Automobile Insurance Company	(93,886)	(125,180)
Income tax effects and adjustments	454,690	586,716
GAAP net income	$2,528,582	$9,871,027

(C) Investment in Blue Chip Stamps

The investment in Blue Chip Stamps by the companies comprising the Insurance Group represented 989,483 shares, or approximately 19% of that company's total outstanding shares at the end of both 1974 and 1973. The carrying value was comprised of the following:

	December 31, 1974	December 31, 1973
Cost, represented by:		
Underlying net asset values at dates of acquisition	$ 9,115,779	$ 9,115,779
Excess cost, net of amortization of $1,279,853, 1974 and $795,673, 1973	2,421,642	2,905,822
	11,537,421	12,021,601
Equity in post-acquisition undistributed earnings	2,833,559	1,695,673
	$14,370,980	$13,717,274

The excess cost over underlying net assets is being amortized over eight years from the beginning of 1972. Amortization charged against earnings of the Insurance Group was $484,180 in 1974 and $480,000 in 1973.

The National Association of Insurance Commissioners assigned per share valuation of $5.25 at December 31, 1974 and $7.25 at December 31, 1973 to the stock of Blue Chip Stamps which is publicly traded in the over-the-counter market. Accordingly, on these bases, the insurance subsidiaries reported in their Convention statements filed with the various state insurance departments an aggregate "market value" of $5,194,784 at December 31, 1974 and $7,171,502 at

Berkshire Hathaway Inc.
INSURANCE GROUP

NOTES TO FINANCIAL STATEMENTS, *Continued*

December 31, 1973, for their holdings of Blue Chip Stamps. The company does not believe that the statutory valuation is indicative of the fair market value of the substantial block of Blue Chip shares represented by the Berkshire Hathaway holdings of which these are a part.

See also note 4 to consolidated financial statements of Berkshire Hathaway Inc. and consolidated subsidiaries.

(D) Stockholders' Equity

The following additional common stock was issued during the two years ended December 31, 1974:

National Indemnity Company, $10 par value common stock:

March 1973 – 150,000 shares of $11,250,000

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

(E) Federal Income Taxes

Federal income tax expense (credit) is made up of the following:

	1974	1973
Totals:		
(Credit) charge applicable to operating earnings	$(2,184,761)	$2,346,719
Charge applicable to equity in earnings of Blue Chip Stamps	99,200	116,000
(Credit) charge applicable to realized investment losses	(567,678)	401,699
	$(2,653,239)	$2,864,418
Current tax expense (credits) relating to:		
Earnings (net operating loss) of insurance underwriting operations	$(1,839,393)	$2,363,435
Dividends received from Blue Chip Stamps	17,200	16,000
Realized investment gains (losses)	(567,678)	401,699
Total current	(2,389,871)	2,781,134

	1974	1973
Deferred tax expense (credit) relating to:		
Equity in undistributed earnings of Blue Chip Stamps	82,000	100,000
Accreted discount on bonds	75,632	170,000
Credit for tax effect of reduction in deferred acquisition costs	(421,000)	(186,716)
Total deferred	(263,368)	83,284
Total income tax expense (credit)	$(2,653,239)	$2,864,418

Total net income (loss) after taking into account realized investment losses, but before income taxes, was ($124,657) for 1974 and $12,735,445 for 1973. Income tax expense (credit) of approximately ($60,000) for 1974 and $6,113,000 for 1973 would result if computed by applying the statutory U. S. Federal income tax rate of 48% to income (loss) before taxes. A reconciliation of the differences are as follows:

	1974	1973
Tax expense at statutory rate	$ (60,000)	$ 6,113,000
Increase (reduction) in income taxes resulting from:		
Tax-exempt interest	(2,082,000)	(2,304,000)
85% dividends received credit relating to:		
Dividends received from unaffiliated companies	(1,065,000)	(542,000)
Equity in earnings of Blue Chip Stamps	(561,000)	(655,000)
Amortization of excess of cost over net assets of subsidiary and investee (not deductible for tax purposes)	277,000	290,000
Tax benefit to affiliate	620,000	–
Capital gains tax rate differential	343,000	(237,000)
Miscellaneous	(125,239)	199,418
	$(2,653,239)	$ 2,864,418

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

The Board of Directors
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, 1974 and 1973, and the related consolidated statements of income, changes in 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, 1974 and 1973, and the results of their operations and 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 17, 1975

Berkshire Hathaway Inc.

BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford

Financial Statements
1974 and 1973

Berkshire Hathaway Inc.
BANK SUBSIDIARY

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

CONSOLIDATED BALANCE SHEETS

	Years ended December 31, 1974	1973
ASSETS		
Cash and due from banks	$ 21,543,577	$ 26,683,653
Investment securities (note 2):		
United States Government obligations	565,107	804,781
United States Government agencies	10,050,113	10,550,049
Obligations of states and political subdivisions	45,857,638	47,712,563
Other securities	3,845,970	3,358,350
Federal funds sold	5,000,000	—
Loans (note 3)	70,853,542	66,022,357
Bank premises and equipment (note 4)	1,008,749	1,116,504
Accrued interest receivable	1,812,021	1,549,003
Other assets	1,044,645	607,074
	$161,581,362	$158,404,334
LIABILITIES RESERVE FOR LOAN LOSSES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Demand deposits	$ 53,177,813	$ 55,716,465
Time deposits	85,519,225	81,450,028
Total deposits	138,697,038	137,166,493
Accrued taxes and other liabilities (note 5)	1,005,234	835,154
Total liabilities	139,702,272	138,001,647
Reserve for loan losses (note 6)	1,251,163	1,163,658
Stockholders' equity:		
Common stock of $20 par value. Authorized and issued 250,000 shares	5,000,000	5,000,000
Surplus	5,000,000	5,000,000
Undivided profits	9,626,927	8,236,029
Reserve for contingencies	1,001,000	1,001,000
Total stockholders' equity	20,627,927	19,239,029
	$161,581,362	$158,404,334

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, 1974	1973
Operating income:		
Interest and fees on loans	$ 6,607,862	$ 5,316,152
Income on Federal funds sold	361,452	236,853
Interest and dividends on:		
United States Government obligations	42,986	47,904
United States Government agencies	898,579	584,272
Obligations of states and political subdivisions	2,797,632	2,795,721
Other securities	284,283	342,642
Total interest income	10,992,794	9,323,544
Trust fees	434,201	456,529
Service charges on deposit accounts	139,060	129,500
Other	559,578	499,862
Total operating income	12,125,633	10,403,435
Operating expenses:		
Interest on deposits	4,954,302	4,295,303
Interest on borrowed money	14,106	55,303
Total interest	4,968,408	4,350,606
Salaries	1,551,511	1,503,374
Employee benefits (note 7)	246,573	262,878
Occupancy, net (note 4)	257,229	417,739
Furniture and equipment (note 4)	248,078	252,709
Provision for loan losses (note 6)	19,300	16,100
Other	592,443	766,862
Total operating expenses	7,883,542	7,570,268
Income before income taxes, securities gains and extraordinary item	4,242,091	2,833,167
Applicable income taxes, net (note 5)	220,256	61,136
Income before securities gains and extraordinary item	4,021,835	2,772,031
Securities gains, net of related taxes of $7,001 in 1974 and $33,939 in 1973 (note 5)	168,022	33,477
Income before extraordinary item	4,189,857	2,805,508
Gain on sale of real estate, net of related taxes of $19,305	—	42,717
Net income	$ 4,189,857	$ 2,848,225

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 CHANGES IN STOCKHOLDERS' EQUITY

	Common stock	*Surplus*	*Undivided profits*	*Reserve for contingencies*
Balance December 31, 1972	$5,000,000	$5,000,000	$ 7,796,349	$1,001,000
Net income	—	—	2,848,225	—
Cash dividends	—	—	(2,300,000)	—
Transfer to reserve for 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
Net income	—	—	4,189,857	—
Cash dividends	—	—	(2,750,000)	—
Transfer to reserve for loan losses, net of tax of $51,122 (note 6)	—	—	(50,959)	—
Balance December 31, 1974	$5,000,000	$5,000,000	$ 9,626,927	$1,001,000

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

	Years ended December 31, 1974	1973
Funds provided:		
Increase in:		
Stockholders' equity:		
Net income	$ 4,189,857	$ 2,848,225
Cash dividends	(2,750,000)	(2,300,000)
Other, net	(50,959)	(106,545)
Net change in stockholders' equity	1,388,898	441,680
Deposits	1,530,545	4,478,197
Other, net	545,570	454,209
Decrease in investment securities	2,106,915	6,130,441
Total	$ 5,571,928	$ 11,504,527
Funds used:		
Increase in loans	9,872,360	6,919,649
Additions to bank premises and equipment	44,891	53,592
Increase in accrued interest receivable	263,018	76,500
Other, net	531,735	(117,392)
	10,712,004	6,932,349
Increase (decrease) in cash and due from banks	(5,140,076)	4,572,178
Total	$ 5,571,928	$ 11,504,527

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, 1974 and 1973

(1) Significant Accounting Policies

The accounting policies of The Illinois National Bank & Trust Co. of Rockford (a 97.7% owned 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 accounting policies:

Consolidation

The consolidated financial statements include those of the Bank and its wholly-owned subsidiary. All significant intercompany transactions are eliminated in consolidation. Certain 1973 amounts have been reclassified to conform with 1974 presentation.

Investment Securities

Investment securities are stated at cost, adjusted for amortization of premium. Accretion of discount is not reflected in the accompanying statements and would not be material. Gains or losses on sales of investment securities are recognized only upon realization and are shown separately in the statements of income.

Installment Loans

Installment loans are generally made on a discount basis. Unearned discount is taken into income over the terms of the respective loans using a method that approximates straight-line.

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.

Costs of major additions and improvements are capitalized. Expenditures for maintenance and repairs are charged against operations as incurred.

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.

Provision for and Reserve for Loan Losses

The provision for loan losses is based on past loan loss experience. Pursuant to regulations of the Comptroller of the Currency, the Bank adopted in 1969 the five-year historical moving average method to determine the minimum annual provision for loan losses charged to operating expense.

(2) Investment Securities

A summary of investments by major classifications is as follows:

	December 31, 1974 (In Thousands)			December 31, 1973 (In Thousands)		
	Par value	*Book value*	*Market value*	*Par value*	*Book value*	*Market value*
U. S. Government—direct	$ 565	$ 565	$ 567	$ 815	$ 805	$ 818
U. S. Government—agencies	10,050	10,050	10,066	10,550	10,550	10,599
State and local municipalities	46,474	45,858	43,778	48,136	47,713	52,057
Other	4,312	3,845	3,550	3,715	3,358	3,453
	$61,401	$60,319	$57,961	$63,216	$62,426	$66,927

The market value decline in investment securities is considered to be a temporary condition in view of the fact that management presently intends to hold the securities to maturity or until they can otherwise be disposed of without significant loss.

Investment securities with a book value of $7,575,779 and $9,530,567 at December 31, 1974 and 1973, respectively, were pledged to secure public deposits and for other purposes.

(3) Loans

A summary of the major classifications of loans at December 31, 1974 and 1973 is as follows:

	1974	*1973*
Commercial loans	$35,706,525	$30,150,101
Consumer credit loans (less unearned discount of $2,722,089 in 1974 and $2,786,609 in 1973)	15,042,339	16,206,182
Floor plan loans	6,211,502	5,312,806
Real estate loans	13,893,176	14,353,268
	$70,853,542	$66,022,357

Berkshire Hathaway Inc.

BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford

AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(4) Bank Premises and Equipment

Bank premises and equipment are recorded at cost less accumulated depreciation of $1,919,822 and $1,777,091 at December 31, 1974 and 1973, respectively. Depreciation expense totaled $146,576 for 1974 and $188,552 for 1973.

(5) Income Taxes

Accrued taxes and other liabilities and the reserve for loan losses in the accompanying balance sheets include deferred taxes of $542,869 and $305,952 at December 31, 1974 and 1973, respectively. Such deferred taxes result from timing differences arising from reporting taxable income on the cash basis. The Bank and its subsidiary join in the filing of a consolidated Federal income tax return with the parent company, Berkshire Hathaway Inc. The tax benefit of deductions by the parent has been passed to the Bank, as shown in the following schedules.

Taxes applicable to net income were as follows:

	1974	*1973*
Tax provision applicable to income before securities gains and extraordinary item	$759,929	$ 61,136
Tax provision applicable to securities gains	88,380	33,939
Tax provision applicable to gain on sale of real estate	–	19,305
	848,309	114,380
Less tax benefit from parent corporation applicable to:		
Income before securities gains	539,673	–
Securities gains	81,379	–
	621,052	–
Applicable income taxes, net	$227,257	$114,380

The components of consolidated income tax expense are as follows:

	1974	*1973*
Taxes currently payable:		
Federal	$466,701	$ 20,364
Less tax benefit from parent applicable to:		
Taxes currently payable	466,701	–
Recovery of prior taxes paid through net operating loss carryback	134,351	–
Total benefit from parent	621,052	–
	(134,351)	20,364
State	124,691	92,268
Total currently payable (receivable)	(9,660)	112,632
Deferred income taxes:		
Federal	222,635	(38,208)
State	14,282	39,956
	236,917	1,748
Applicable income taxes, net	$227,257	$114,380

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

	1974	*1973*
Net increase in accrued income taken on cash basis on tax return and on accrual basis for books	$156,825	$101,402
Net (increase) decrease in accrued expenses taken on cash basis on tax return and accrual basis for books	28,970	(104,094)
Loan loss deduction on tax return in excess of the amount charged to operating expenses	51,122	4,440
	$236,917	$ 1,748

Total tax expense amounted to $227,257 (an effective rate of 5.1%) in 1974, and $114,380 (an effective rate of 4.0%) in 1973, a total less than $2,120,215 and $1,368,778 for 1974 and 1973, respectively, computed by applying the United States Federal income tax rate of 48% to income before tax. The reasons for these differences are as follows:

	1974		1973	
	Amount	*Percent of pretax income*	*Amount*	*Percent of pretax income*
Tax expense at statutory rate	$2,120,215	48.0%	$1,368,778	48.0%
Increase (reduction) in taxes resulting from:				
Tax-exempt interest	(1,342,863)	(30.4)	(1,341,946)	(47.1)
State income taxes, net of Federal income tax benefits	72,266	1.6	68,756	2.4
Tax benefit from parent	(621,052)	(14.1)	–	–
Other—net	(1,309)	–	18,792	.7
Actual tax expense	$ 227,257	5.1%	$ 114,380	4.0%

Berkshire Hathaway Inc.

BANK SUBSIDIARY

The Illinois National Bank & Trust Co. of Rockford

AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, *Continued*

(6) Reserve for Loan Losses

The following schedule summarizes the changes in the reserve for loan losses for the years ended December 31, 1974 and 1973:

	1974	1973
Balance at beginning of year	$1,163,658	$1,024,601
Recoveries on loans previously charged off	7,299	29,143
Provisions charged to:		
Operating expenses	19,300	16,100
Undivided profits	50,959	106,545
Deferred income taxes	51,122	4,440
	1,292,338	1,180,829
Less loans charged off	41,175	17,171
Balance at end of year	$1,251,163	$1,163,658

The portion of the reserve which was available to absorb possible loan losses was $719,919 at December 31, 1974 and $734,495 at December 31, 1973.

The components of the reserve for loan losses as of December 31, 1974 and 1973 are as follows:

	1974	1973
Valuation (available for charging off loan losses)	$ 719,919	$ 734,495
Contingency (undivided profits)	313,742	262,783
Deferred taxes	217,502	166,380
	$1,251,163	$1,163,658

(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 total expense was $128,247 for 1974 and $144,559 for 1973.

Based upon the most recent actuarial report available (as of January 1, 1974), the pension fund assets exceeded the actuarial computed value of vested benefits; and there was no unfunded past service cost liability.

Berkshire Hathaway Inc.

LINES OF BUSINESS

Sources of Revenues:

Revenues reflected in the consolidated financial statements include those from (1) premiums earnings and investment income of the Insurance Group, plus (2) sales revenues from the textile business of the parent company and its Canadian subsidiary plus a minor amount of investment income of the parent company. The following table summarizes for the past five years the total revenues derived from these two categories for the past five years, in thousands of dollars:

	1970	1971	1972	1973	1974
Insurance	$42,249	$66,050	$66,556	$60,526	$ 68,776
Textile	24,629	26,092	27,772	33,479	32,706
	$66,878	$92,142	$94,328	$94,005	$101,482

Sources of Net Income:

The unconsolidated bank subsidiary and the investment in Blue Chip Stamps represent additional significant sources of income for the Company. Sources of total net income for the past five years, on a pre-tax basis with total tax effects to the Company and its consolidated subsidiaries reflected as a separate item, were as follows for the past five years:

	(Thousands of Dollars) 1970	1971	1972	1973	1974
Insurance	$2,639	$6,372	$10,701	$10,249	$ 892
Textile	104	233	1,697	2,837	2,660
Unconsolidated bank subsidiary	2,973	2,192	2,700	2,782	4,093
Blue Chip Stamps	—	68	142	1,124	1,164
Interest and corporate administrative expenses	(581)	(648)	(770)	(1,966)	(2,324)
Realized investment gain (loss)	(301)	1,028	1,359	1,331	(1,908)
Extraordinary item	282	—	—	—	—
Total pre-tax income	5,116	9,245	15,829	16,357	4,577
Less: Total income taxes (credit)	551	1,559	3,703	3,497	(2,466)
Net Earnings	$4,565	$7,686	$12,126	$12,860	$7,043

Berkshire Hathaway Inc.

FIVE YEAR SUMMARY OF OPERATIONS

	1970	1971	1972	1973	1974
	(Dollars in thousands, except per share amounts)				
Insurance premiums earned	$39,172	$60,867	$59,627	$52,929	$60,574
Net sales of textile products	24,569	26,011	27,742	33,411	32,592
Interest and dividend income	2,942	5,043	6,648	7,378	8,030
Insurance underwriting gain (loss)	(331)	1,409	4,284	3,319	(6,892)
Gross profit from sales of textile products	2,349	2,566	4,087	5,105	5,163
Interest expense	581	595	584	1,605	1,718
Income taxes (credit) applicable to insurance underwriting and textile operations	387	1,245	3,241	2,979	(2,010)
Net earnings from insurance underwriting and textile operations	1,675	4,712	8,387	8,141	3,239
Equity in net earnings of bank subsidiary	2,973	2,192	2,700	2,782	4,093
Equity in net earnings of Blue Chip Stamps	—	63	111	1,008	1,052
Earnings before realized investment gains (losses) and extraordinary items	4,648	6,967	11,198	11,931	8,383
Realized investment gains (losses) net of income taxes	(301)	719	928	929	(1,340)
Net earnings	4,565	7,686	12,126	12,860	7,043
Average shares outstanding	979,715	979,569	979,569	979,569	979,569
Per share:					
Earnings before realized investment gains (losses) and extraordinary items	4.74	7.11	11.43	12.18	8.56
Net earnings	4.66	7.85	12.38	13.13	7.19

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE SUMMARY OF OPERATIONS

Insurance Premiums Earned and Insurance Underwriting Gain (Loss)

The following table sets forth the net premiums written and earned by the Insurance Group in each of the past three years:

Operational Area		*1972*	*1973*	*1974*
		(Thousands of Dollars)		
Specialized Auto, General Liability and Other(1)	Written	$35,354	$28,617	$36,738
	Earned	37,950	29,969	34,436
Reinsurance(2)	Written	11,436	10,184	12,204
	Earned	11,699	11,996	12,938
Urban Auto(3)	Written	6,874	6,571	6,613
	Earned	7,092	6,120	7,902
Home State Companies(4)	Written	4,286	5,000	5,442
	Earned	2,886	4,844	5,298
Totals	Written	$57,950	$50,372	$60,997
	Earned	$59,627	$52,929	$60,574

(1) National Indemnity Company and National Fire & Marine Insurance Company less the Reinsurance Department of National Indemnity.

(2) Reinsurance Department of National Indemnity.

(3) Home and Automobile Insurance Company.

(4) Corporations organized in the jurisdictions of Nebraska, Minnesota, Texas and Iowa underwriting standard and preferred classes of fire and casualty insurance in those states.

Premium volume, both written and earned, in National Indemnity's most significant line of insurance, i.e., substandard private passenger automobile and commercial automobile coverages, is subject to significant fluctuation from year to year. This is a highly competitive area, as is the area of general liability also underwritten by National Indemnity. General liability premiums written by National Indemnity declined from the preceding year by approximately $1 million in both 1973 and 1974. This decline in 1974 was offset by increased writings of workmen's compensation coverages. Private passenger and commercial auto underwritings declined by approximately $7 million from 1972 to 1973; this loss in volume was substantially recovered in 1974.

Combined loss and expense ratios (which are the sum of the ratio of losses and loss expenses incurred to premiums earned plus the ratio of underwriting expenses to premiums written) have been as follows for the Insurance Group for the past five years.

	NET PREMIUMS		RATIOS		
	Written (In thousands)	Earned	Losses and Loss Adj. Exp./ Earned Prem.	Underwriting Expenses/ Written Prem.	Combined Loss and Expenses Ratio
1970	$45,086	$39,172	68.6%	31.7	100.3
1971	66,455	60,867	67.0	30.1	97.1
1972	57,950	59,627	62.0	29.7	91.7
1973	50,372	52,929	62.0	32.5	94.5
1974	60,997	60,574	77.8	32.0	109.8

The combined loss and expense ratio is the traditional measure of underwriting results of property and casualty companies. In any year when that ratio exceeds 100, it generally indicates that unprofitable business has been underwritten.

The total underwriting gain or loss for the Insurance Group for the past three years is shown in the following table:

	(Thousands of Dollars)					
	1972		1973		1974	
	Statutory	*GAAP*	*Statutory*	*GAAP*	*Statutory*	*GAAP*
Specialized auto, general liability and other	$5,530	$4,329	$4,623	$4,409	$(2,119)	$(1,939)
Reinsurance	614	561	715	353	(1,470)	(2,068)
Urban Auto	86	62	(834)	(878)	(1,761)	(2,183)
Home state companies	(798)	(667)	(801)	(565)	(702)	(702)
	$5,432	$4,285	$3,703	$3,319	$(6,052)	$(6,892)

The only difference between the Statutory and GAAP underwriting results is the change in amount of premium acquisition costs (underwriting expenses, i.e., commissions, etc.) which is deferred under GAAP. In each of the above years, the amount of such costs deferred at year-end decreased from the preceding year-end. The decrease of $840,000 in deferred acquisition costs in 1974 was generally in recognition of unfavorable underwriting results expected from certain portions of the in-force book of business, plus, in the case of Home and Auto, where no costs were deferred at December 31, 1974, a recognition of substantially reduced premium volume without yet having achieved commensurate reduction in operating expenses.

The premium rates at which the Insurance Group wrote its business in 1974 proved inadequate. Premium rate increases lagged the rate of inflation in both 1973 and 1974, and, while the industry in general and the Berkshire Insurance Group in particular escaped the expected consequences in 1973, they suffered quite badly in 1974.

In addition to the negative influence on the Insurance Group of inadequate rates to cover inflating claim costs, the reinsurance operations in 1974 sustained what management considers to have been an above average number of catastrophe loss occurrences related to the April tornadoes in the country. In contrast, management believes that its catastrophe loss occurrences in 1973 were below average in number.

The "Urban Auto" business referred to above, conducted by Home and Automobile Insurance Company ("Home and Auto") differs from that of National Indemnity and National Fire & Marine principally in that rates and other aspects of Home and Auto's business are based almost entirely upon the loss experienced in the limited urban area in which it operates. These operations were limited to the Chicago area until 1973 when a similar operation was begun in the Miami area. Premium volume from this Florida operation was only nominal in 1973, but approximated $1,700,000, or 25% of Home and Auto's 1974 net written premiums. This proved unprofitable, a statutory underwriting loss of approximately $1,600,000 was sustained in 1974 on this Florida business, and underwriting in Florida by Home and Auto was terminated in 1974. Losses incurred there are still in process of settlement. Home and Auto's underwriting loss in 1973 was attributable to its Cook County, Illinois business which had historically been profitable. Premium rate increases were effected for the Chicago area writings in the fourth quarter of 1974. This resulted in somewhat lower premium writings in this traditional area of Home and Auto's business in 1974, and it is expected that a significantly lower level of premiums will be written in all of 1975.

Net Sales and Gross Profit from Sales of Textile Products

Efforts to optimize product sales mix have been continuously underway during the last five years in the textile operations. These efforts tend to be most rewarding when demand for all products is strong as it was in 1972, 1973 and during the first three quarters of 1974. The lack of availability of certain desired raw materials was a minor deterrent to these efforts in early 1974. The shortages were, we believe, attributable to distortions existing in the economy generally and have not persisted. In late 1974 demand for our products fell to depressed levels; the major impact of this will be reflected in lower sales and gross profits in 1975.

1973 compared to 1972: Total sales of textile products in 1973 increased over 1972 by approximately 20% measured in dollars, and 14% measured in yards. The increase in unit sales was achieved in a profitable area and this, combined with inflation, caused stated gross profits in 1973 to increase by 25% over 1972. See Note 7 to the consolidated financial statements which discloses the effect on 1973 earnings of the change in that year to the LIFO basis of determining cost of inventories.

1974 compared to 1973: In 1974, unit sales of textile products declined approximately 14% from 1973; but improved product mix and higher selling prices influenced in large part by inflation allowed dollar sales and gross profits to remain almost level with 1973.

Interest and Dividend Income

Interest and dividend income is earned almost entirely by the Insurance Group. The continuing increase in this category of income is the result of increased investments. Interest and dividend income is related to average investments for the past five years in the following table, which excludes the investment in and dividends received from Blue Chip Stamps, which is accounted for by the equity method.

	Average Investments at cost	*Interest and Dividend Income*	*Average Per Cent Earned*
	(Amounts in Thousands)		
1970	51,422	2,942	5.72
1971	79,117	5,043	6.37
1972	103,217	6,648	6.44
1973	117,516	7,378	6.28
1974	131,347	8,030	6.11

The average per cent earned declined in 1973 and 1974 as a result of the increase in the average investments in preferred and common stocks relative to the average investment in bonds; the income yield on the bonds tends to exceed that on the stocks. Investments for the past five years are categorized in the following table, at the average of their carrying values at the beginning and end of each year:

	Bonds, Treasury bills and other short-term obligations	*Preferred and common stocks*	*Total*
		(In Thousands of Dollars)	
1970	41,722	9,700	51,422
1971	68,906	10,211	79,117
1972	87,175	16,042	103,217
1973	81,311	36,205	117,516
1974	78,557	52,790	131,347

Interest Expense

The significant increase in interest expense in 1973, as compared to 1972, is attributable to the increase in indebtedness outstanding as a result of issuance in March of 1973 of $20,000,000 8% Senior Notes due 1993. Part of the proceeds of that financing was used to repay $9,000,000 of bank notes which were outstanding in 1972, with respect to which the effective interest rate had been less than 7%.

Income Taxes (Credit) Applicable to Insurance Underwriting and Textile Operations

Each year there is a significant difference between pre-tax income reported in the financial statements, and income subject to tax. The difference arises principally from certain dividends received credits and from the fact that a considerable portion of income of the Insurance Group is produced by tax exempt bonds. For 1974, these items exceeded the pre-tax earnings from insurance underwriting and manufacturing operations and all other items of taxable income so that a "net operating loss", as defined by the Internal Revenue Code, was reported for tax purposes. Berkshire Hathaway Inc. and its includible subsidiaries join in the filing of a consolidated Federal income tax return, and the 1974 consolidated net operating loss can be carried back to recover income taxes paid by members of the group for 1971 and 1972. Consequently, an income tax credit to earnings for 1974 appears in the summary of earnings, compared to an income tax expense for preceding years.

Equity in Net Earnings of Bank Subsidiary

Berkshire's equity in net earnings of the Illinois National Bank and Trust Co. of Rockford, a 98% owned subsidiary of Berkshire, increased to $4,093,000 in 1974, an increase of $1,311,000, or 47%, over the $2,782,000 recorded for 1973. The bank incurred no current Federal income tax expense for 1974, benefiting, as a member of the group for which Berkshire files a consolidated Federal income tax return, from the net operating losses sustained by other members of the group. Increases in the banks pre-tax earnings thus virtually became increases in its net earnings.

Income of the bank before income taxes and before securities transactions increased $1,409,000, or 49.7%, over 1973. The sources of this change were as follows (dollars in thousands):

			Change	
	1974	*1973*	*Amount*	*%*
Interest income	$10,993	$9,324	$1,669	17.9
Interest expense	4,969	4,351	618	14.2
Net interest earnings	6,024	4,973	1,051	21.1
Non-interest income	1,133	1,080	53	4.9
	7,157	6,053	1,104	18.2
Non-interest expenses	2,915	3,220	(305)	(9.5)
Income before taxes and before securities transactions	$ 4,242	$2,833	$1,409	49.7

Loan demand continued strong throughout the year and was accompanied by record high interest rates. Accordingly, interest income increased as a result of increased volume of earning assets and a higher yield thereon. Increased reliance on interest bearing time deposits as a source of funds and an increased average rate paid thereon caused the rise in interest expense.

Non-interest expense items declined in total primarily as the result of a change instituted by local taxing authorities in assessing to Berkshire, as a shareholder of the bank, certain capital stock taxes previously assessed to the bank. While bank earnings increased as a result of this action by the taxing authorities, the net effect of this change was of no benefit to Berkshire, since taxes not heretofore paid by Berkshire amounting to approximately $260,000 appear as part of Berkshire's 1974 selling and administrative expenses.

Equity in Net Earnings of Blue Chip Stamps

Berkshire's equity in net earnings of Blue Chip Stamps as computed by the equity method for each of the past three years has been as follows:

	1972	*1973*	*1974*
	(Amounts in Thousands)		
Equity in net earnings	$458	$1,605	$1,548
Applicable income taxes	(31)	(116)	(112)
Amortization of excess of cost over equity in net assets	(316)	(481)	(384)
Net equity in earnings	$111	$1,008	$1,052

The number of shares of Blue Chip Stamps owned by Berkshire has increased in each of the past three years. Average shares owned in 1972, 1973 and 1974 were, respectively, 464,527, 934,000, and 1,144,670. Stated on the basis of per-average-share-owned, the above table is as follows:

	1972	1973	1974
Equity in net earnings	$0.99	$1.72	$1.35
Applicable income taxes	(.07)	(.12)	(.10)
Amortization of excess of cost over equity in net assets	(.68)	(.52)	(.33)
Net equity in earnings	$0.24	$1.08	$0.92

Realized Investment Gains (Losses)

Realized investment losses in 1974 aggregated $1,908,000 with a tax carryback credit of $568,000 reducing the after-tax realized investment loss to $1,340,000. In 1973 and 1972 realized investment gains before taxes were, respectively, $1,332,000 and $1,359,000; after taxes, $929,000 and $928,000. Realization of investment gains or losses is determined by prevailing investment strategy as applied under changing economic conditions.

Unrealized market value decreases in investments in preferred and common stocks of unaffiliated companies amounted to $4,356,000 in 1974 and $13,741,000 in 1973, contrasted with a nominal $272,000 increase in 1972. In the absence of operating or investment reasons compelling liquidation, we consider it inappropriate to reflect in income the results of temporary fluctuations in market value of investments; consequently, unrealized investment losses or gains do not appear in the summary of earnings.

During the first ten weeks of 1975, the company realized investment losses of approximately $1,500,000, net of applicable tax credit. Also during the first ten weeks of 1975 management noted a recovery exceeding $10,000,000 in market value of its preferred and common stock portfolio. Neither the lasting effect, total timing nor extent of this recovery in market values can be predicted, but management believes that over the long term, no significant net loss to the company will result from its continued holding or sale of the securities which constituted its portfolio at December 31, 1974.

Berkshire Hathaway Inc.

DIRECTORS AND EXECUTIVE OFFICERS

WARREN E. BUFFETT, *Director and Chairman of the Board*
Chief Executive Officer of the Company

KENNETH V. CHACE, *Director*
President of the Company and Chief Operating Officer of the Textile Operations of the Company

MALCOLM G. CHACE, JR., *Director*
Retired, Former Chairman of the Board of Directors

J. VERNE MCKENZIE, *Director*
Vice President, Secretary and Treasurer of the Company

COMMON STOCK PRICES

The common stock of Berkshire Hathaway Inc. is traded in the over the counter market. The high and low bid prices for the stock in each quarter of 1973 and 1974 is set forth in the following table:

		High	Low
1973	1st Quarter	93	80
	2nd Quarter	87	85
	3rd Quarter	88	83
	4th Quarter	87	71
1974	1st Quarter	76	72
	2nd Quarter	76	64
	3rd Quarter	64	49
	4th Quarter	49	40

The Company has not paid a dividend in the past two years.

Annual Report for 1975

BLUE CHIP
STAMPS

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Financial Highlights

(In thousands except for amounts per share)

	Fiscal year ended March 1, 1975	Fiscal year ended March 2, 1974	Quarter ended March 1, 1975	Quarter ended March 2, 1974
Stamp service revenues	$25,564	$ 51,375	$ 5,862	$ 8,774
Merchandise promotions and incentive sales	11,022	6,261	2,719	1,317
Candy sales	42,907	35,780	21,220	17,572
Other revenues	9,872	8,803	2,797	2,672
Total revenues	$89,365	$102,219	$32,598	$30,335
Income before equity in net income of Wesco Financial Corporation, securities gains (losses) and extraordinary credit	$ 5,377	$ 6,767	$ 2,378	$ 2,772
Equity in net income of Wesco Financial Corporation	2,131	1,423	319	452
Income before securities gains (losses) and extraordinary credit	7,508	8,190	2,697	3,224
Securities gains (losses), less income taxes	254	(185)	826	(398)
Extraordinary credit	903	—	790	—
Net income	$ 8,665	$ 8,005	$ 4,313	$ 2,826
Per share:				
Income before securities gains (losses) and extraordinary credit	$ 1.45	$ 1.58	$.52	$.62
Net income	$ 1.67	$ 1.55	$.83	$.55
Book value	$13.00	$11.56		

To Our Stockholders

Net income increased $.12 per share to $8,665,000 or $1.67 per share for the fiscal year ended March 1, 1975 The current per share figure includes securities gains of $.05 and an extraordinary credit of $.17, compared to securities losses of $.03 for the prior fiscal year.

Earnings before securities transactions and the extraordinary credit totaled $7,508,000 or $1.45 per share for the current fiscal year, down $.13 from a year ago.

A substantial portion of the securities gains this year were realized during the fourth quarter resulting in a substantial increase in the extraordinary credit, which represents the amount of federal income tax on capital gains that will not be payable due to utilization of capital loss carry-forwards.

Stamp service revenues again declined substantially from those generated in the preceding year. Total revenues dropped to a lesser extent due to increases in sales of See's candy and in other categories of revenue.

See's Candy Shops, Incorporated had a record year, by a substantial margin, in profits as well as sales, under the very capable leadership of Charles Huggins.

Blue Chip's equity in net income of Wesco Financial Corporation increased sharply as a result of a substantial increase in ownership, which is now 64%. Wesco's earnings declined, generally following the profit trend for the savings and loan industry.

We have expanded the annual report this year to comply with new government regulations. Rather than repeat here numerous other explanations of changes in our business, we direct your attention to the sections entitled Principal Business Activities and Summary of Operations.

Revenues in our original business, trading stamps, have declined approximately 80% in the last five years. This severe decline in volume could not be foreseen. We take pride in our adjustment to adversity over the last few years. You will note, for example, that the $40,000,000 in bank loans that appeared on the March 2, 1974 consolidated balance sheet has been repaid and our outstanding debentures have been substantially reduced. We will continue to seek ways to build and maintain the value of your investment in the Company.

Cordially yours,

Donald A. Koeppel

Donald A. Koeppel
Chairman of the Board and
President

April 14, 1975

Principal Business Activities

Blue Chip Stamps (the "Company") and its subsidiaries are engaged in four lines of business:

(1) **The trading stamp business.** The Company provides a trading stamp service to retail merchants and their customers in California and Nevada. The service includes the issuance of trading stamps, catalogs, savings books, signs, banners and other promotional material as well as the redemption of Blue Chip stamps for merchandise or cash through sixty-five redemption stores.

(2) **The incentive and merchandise promotion business.** 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.

(3) **The candy business.** See's Candy Shops, Incorporated, a 99%-owned subsidiary acquired in January 1972, produces quality candy and confectionery products in two fully equipped kitchens in California. The candy is sold fresh to the public in 170 company-operated shops in nine western states including Hawaii. The See's entity is believed to be one of the largest candy manufacturers distributing through its own chain of retail shops. Chocolate, sugar and certain other essential ingredients are generally available but subject to price fluctuations from time to time. A substantial portion of each year's candy sales are generated during the Christmas season.

(4) **The savings and loan business.** Wesco Financial Corporation, an unconsolidated subsidiary controlled since late 1973, owns all of the outstanding guarantee stock of Mutual Savings and Loan Association, which operates at thirteen locations in Southern California. The association is engaged in the business of lending money, principally secured by first liens against real estate, to enable borrowers to purchase, construct or refinance real property.

Stamp service revenues have declined from a historical peak of $124,180,000 for the fiscal year ended February 28, 1970 to $25,564,000 for the fiscal year ended March 1, 1975. This decline has resulted primarily from two factors. First, a number of supermarket operators discontinued or reduced the use of trading stamps in connection with their conversion to discount merchandising. Second, the service station industry, as a result of the gasoline shortage, virtually eliminated the use of stamps. The reduction in stamp revenues has increased the relative importance to the business of the remaining customers; the three largest customers, all Southern California supermarket chains, accounted for 27% of stamp volume during the fiscal year ended March 1, 1975 as compared with 12% the preceding year. Over the past three years the Company has reduced the number of redemption stores from a peak of 90 to 65 at present. The number of its employees fluctuates but now averages less than 600.

The following table sets forth the relative contribution of each line of business presently accounting for ten per cent or more of total (consolidated) revenues or of total income before income taxes, securities gains (losses) and extraordinary items for the five fiscal years ended March 1, 1975:

	1975	1974	1973	1972	1971
Revenues:					
Trading stamp service	39%	59%	73%	95%	99%
Incentive and merchandise promotions	12	6	2	1	1
Candy business	49	35	25	4	—
Income (loss) before income taxes, securities gains (losses) and extraordinary items:					
Trading stamp service	—	44	60	95	100
Incentive and merchandise promotions	(7)	—	2	1	—
Candy business	77	40	38	4	—
Savings and loan business	30	16	—	—	—

Summary of Operations

Five Fiscal Years Ended March 1, 1975
(In thousands except for amounts per share)

	1975	1974	1973	1972	1971
Revenues:					
Stamp service revenues	$ 25,564	$ 51,375	$ 88,736	$100,622	$118,374
Merchandise promotions and incentive sales	11,022	6,261	3,624	2,145	1,759
Candy sales	42,907	35,780	32,049	4,104	—
Dividends and interest	7,738	8,260	7,315	6,359	6,203
Other	2,134	543	599	872	1,448
	89,365	102,219	132,323	114,102	127,784
Costs and expenses:					
Cost of redemptions and sales	54,912	68,156	95,662	93,791	104,392
Selling, general and administrative expenses	23,483	21,263	21,729	10,917	8,558
Interest	4,050	3,597	2,638	927	705
Discount amortization	306	365	358	365	358
	82,751	93,381	120,387	106,000	114,013
Income before income taxes, equity in net income of Wesco Financial Corporation, securities gains (losses) and extraordinary items	6,614	8,838	11,936	8,102	13,771
Provision for income taxes	(1,237)	(2,071)	(3,828)	(2,195)	(5,032)
Equity in net income of Wesco Financial Corporation	2,131	1,423	—	—	—
Income before securities gains (losses) and extraordinary items	7,508	8,190	8,108	5,907	8,739
Securities gains (losses), less income tax effect	254	(185)	(82)	(1,693)	(155)
Income before extraordinary items	7,762	8,005	8,026	4,214	8,584
Extraordinary credit (charges)	903	—	(925)	—	—
Net income	$ 8,665	$ 8,005	$ 7,101	$ 4,214	$ 8,584
Per share:					
Income before securities gains (losses) and extraordinary items	$1.45	$1.58	$1.58	$1.15	$1.72
Securities gains (losses), less income tax effect	.05	(.03)	(.02)	(.33)	(.03)
Income before extraordinary items	1.50	1.55	1.56	.82	1.69
Extraordinary credit (charges)	.17	—	(.18)	—	—
Net income	$1.67	$1.55	$1.38	$ .82	$1.69
Dividends declared	$ .24	$ .24	$ .24	$ .24	$ .24

Summary of Operations

Notes to Summary of Operations

Candy sales and other accounts of the candy subsidiary are included on a consolidated basis from acquisition in January 1972.

The Company's equity in Wesco Financial Corporation's net income is included under the equity method beginning with the fiscal year ended March 2, 1974 (see Note 1 to the accompanying consolidated financial statements).

The extraordinary charges for the year ended March 3, 1973 represented settlement of lawsuits, less income tax effect. The extraordinary credit for the year ended March 1, 1975 represented the amount of federal income tax which is not payable due to offset of capital loss carry-forwards, primarily from the year ended March 4, 1972.

Management's Discussion and Analysis of the Summary of Operations

The decline in stamp service revenues throughout the five-year period ended March 1, 1975 has been caused by various factors as explained above under Principal Business Activities.

Revenues from merchandise promotions and incentive sales have increased sharply during the two years ended March 1, 1975 primarily as a result of the Company's diversification into developing, for oil companies and other large issuers of credit cards, complete merchandise packages for their credit card holders.

Candy sales increased from fiscal 1973 to fiscal 1974 due to modest increases in average price per pound and number of pounds sold. The increase in fiscal 1975 resulted from substantial further improvement in the pricing structure.

The increase in dividend and interest income from fiscal 1973 to fiscal 1974 was mainly the result of improved yield on equity securities.

Other revenues in fiscal 1975 included a $1,254,000 gain on sale of the Company's Richmond, California warehouse and a $311,000 gain on purchase and early retirement of outstanding debentures.

Cost of redemptions and sales during the two years ended March 1, 1975 was generally commensurate with related revenues.

The increase in selling, general and administrative expenses from fiscal 1974 to fiscal 1975 was due mainly to a slight overall increase in employee compensation as well as an increase in commissions paid with respect to credit card merchandise promotions.

The sharp rise in interest expense during fiscal 1974 and 1975, despite a slight reduction in average loan balances over the period, was caused principally by increases in the prime interest rate upon which loan interest was based.

The provision for income taxes declined as a percentage of pre-tax income from 32% in fiscal 1973 to 23% in fiscal 1974 due to an increase in dividend income, most of which is 85% excludable in computing federal taxable income. The effective rate dropped further to 19% in fiscal 1975 because excludable dividends, although reduced, represented a greater proportion of pre-tax income.

The Company's equity in net income of Wesco Financial Corporation increased from fiscal 1974 to fiscal 1975 due to a substantial increase in ownership, which is now 64%. Wesco's earnings declined.

Securities gains and losses fluctuate from year to year and accordingly are set out separately. The after-tax change from net losses of $185,000 in fiscal 1974 to net gains of $254,000 in fiscal 1975, although material, was not abnormal to the business.

Revenues, expenses, earnings and other items set forth on the summary of operations are not necessarily indicative of future revenues, expenses, earnings and other items. In particular, stamp service revenues have declined over the past five years and the contribution of the trading stamp business to pre-tax earnings over the same period has declined to nil (see Principal Business Activities). As indicated in Note 10 to the accompanying consolidated financial statements, the Company believes that a sale or spin-off of one-third of its California trading stamp business, if consummated under existing market conditions, would compel it to discontinue issuance of trading stamps. However, the Company now considers forced consummation of any sale or spin-off unlikely.

Report of Independent Accountants

Price Waterhouse & Co.

606 SOUTH OLIVE STREET, LOS ANGELES, CALIFORNIA 90014
213-623-2131

April 14, 1975

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 1, 1975 and March 2, 1974, and the related consolidated statements of income and retained earnings and of 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 10 to the accompanying consolidated 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 1, 1975 and March 2, 1974 and the results of their operations and the changes in financial position for the fiscal years then ended, in conformity with generally accepted accounting principles consistently applied.

Price Waterhouse & Co.

Consolidated Balance Sheet

Blue Chip Stamps

March 1, 1975 and March 2, 1974 (Note 1)

	1975	1974
ASSETS		
Cash	$ 1,506,000	$ 3,013,000
Marketable securities, at cost (market value, $59,594,000 at March 1, 1975 and $128,654,000 at March 2, 1974) (Note 3)	77,541,000	132,743,000
Accounts receivable	5,529,000	4,034,000
Merchandise and supplies inventories, at the lower of cost (first-in, first-out) or market	11,767,000	10,355,000
Prepaid income taxes and other expenses (Note 7)	6,689,000	5,861,000
Property, fixtures and equipment, net (Note 4)	8,273,000	10,454,000
Investment in Wesco Financial Corporation (Note 1)	26,307,000	17,446,000
Excess of cost over equity in net assets of See's Candy Shops, Incorporated, less accumulated amortization (Note 1)	15,883,000	16,314,000
	$153,495,000	$200,220,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable and accrued expenses	$ 5,489,000	$ 8,146,000
Income taxes payable (Note 7)	2,002,000	2,858,000
Liability for unredeemed trading stamps (Note 2)	72,183,000	78,776,000
Notes payable to bank	—	40,000,000
6¾% Subordinated Debentures due 1978 (Note 5)	6,512,000	10,553,000
	86,186,000	140,333,000
Stockholders' equity (Notes 5, 7, 8 and 10):		
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	60,551,000	53,129,000
Total stockholders' equity	67,309,000	59,887,000
	$153,495,000	$200,220,000

See accompanying notes to consolidated financial statements

Consolidated Statement of Income and Retained Earnings

Blue Chip Stamps

Fifty-two Weeks Ended March 1, 1975 and March 2, 1974 (Note 1)

	1975	1974
Revenues:		
Stamp service revenues (Note 2)	$ 25,564,000	$ 51,375,000
Merchandise promotions and incentive sales	11,022,000	6,261,000
Candy sales	42,907,000	35,780,000
Dividends and interest	7,738,000	8,260,000
Other revenues (Notes 4 and 5)	2,134,000	543,000
	89,365,000	102,219,000
Costs and expenses:		
Cost of redemptions and sales (Note 2)	54,912,000	68,156,000
Selling, general and administrative expenses	23,483,000	21,263,000
Interest and discount amortization	4,356,000	3,962,000
	82,751,000	93,381,000
Income before income taxes, equity in net income of Wesco Financial Corporation, securities gains (losses) and extraordinary credit	6,614,000	8,838,000
Provision for income taxes (Note 7)	(1,237,000)	(2,071,000)
Equity in net income of Wesco Financial Corporation (Notes 1 and 7)	2,131,000	1,423,000
Income before securities gains (losses) and extraordinary credit	7,508,000	8,190,000
Securities gains (losses), less income tax effect (Note 7)	254,000	(185,000)
Extraordinary credit (Note 7)	903,000	—
Net income	8,665,000	8,005,000
Retained earnings at beginning of year	53,129,000	46,367,000
Cash dividends of $.24 per share per year (Note 5)	(1,243,000)	(1,243,000)
Retained earnings at end of year	$ 60,551,000	$ 53,129,000
Amounts per share based on weighted average shares outstanding:		
Income before securities gains (losses) and extraordinary credit	$1.45	$1.58
Securities gains (losses)	.05	(.03)
Extraordinary credit	.17	—
Net income	$1.67	$1.55

See accompanying notes to consolidated financial statements

Consolidated Statement of Changes in Financial Position

Blue Chip Stamps

Fifty-two Weeks Ended March 1, 1975 and March 2, 1974 (Note 1)

	1975	1974
Sources of cash:		
Income before extraordinary credit	$ 7,762,000	$ 8,005,000
Add (deduct) items not requiring (providing) cash:		
Depreciation and amortization	1,582,000	1,931,000
Increase in prepaid income taxes and other expenses	(1,216,000)	(91,000)
Equity in net income of Wesco Financial Corporation less dividends received, net of income taxes	(1,379,000)	(1,004,000)
Cash provided by operations before extraordinary credit	6,749,000	8,841,000
Extraordinary credit — federal income tax not payable due to offset of capital loss carry-forwards	903,000	—
Decrease in marketable securities	55,202,000	11,858,000
Decrease (increase) in property, fixtures and equipment	961,000	(1,022,000)
Total	63,815,000	19,677,000
Uses of cash:		
Decrease (increase) in notes payable to bank	40,000,000	(10,245,000)
Purchase of debentures for retirement	4,041,000	287,000
Purchase of stock of Wesco Financial Corporation	7,025,000	16,224,000
Payment of dividends	1,243,000	1,243,000
Increase (decrease) in accounts receivable	1,495,000	(114,000)
Increase (decrease) in merchandise and supplies inventories	1,412,000	(2,759,000)
Decrease in accounts payable	2,657,000	480,000
Decrease in income taxes payable	856,000	1,169,000
Decrease in liability for unredeemed trading stamps	6,593,000	14,575,000
Total	65,322,000	20,860,000
Decrease in cash	$ (1,507,000)	$ (1,183,000)

See accompanying notes to consolidated financial statements

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 in each of the fiscal years ended in 1975 and 1974.

The Company's investment in Wesco Financial Corporation (Wesco), a savings and loan holding company, has increased from 21.9% at March 3, 1973 to 44.6% at March 2, 1974 and 64.4% at March 1, 1975. The investment is recorded at cost plus equity in Wesco's calendar-year net income, less taxes; the $18,699,000 and $12,562,000 excess of equity in the net assets of Wesco over cost at March 1, 1975 and March 2, 1974, respectively, is being amortized over 40 years. Such amortization amounted to $457,000 and $218,000 during the fiscal years ended in 1975 and 1974. Summarized financial information of Wesco for the years ended December 31, 1974 and 1973 follows:

	December 31, 1974	December 31, 1973
Assets—		
Cash and marketable securities	$ 53,065,000	$ 40,112,000
Loans receivable, less unearned loan fees, unrealized profit and loans in process	389,065,000	389,584,000
Other assets	23,516,000	22,284,000
	$465,646,000	$451,980,000
Liabilities and stockholders' equity—		
Savings deposits	$333,117,000	$345,530,000
Other liabilities	62,238,000	38,899,000
Total liabilities	395,355,000	384,429,000
Stockholders' equity, partially appropriated	70,291,000	67,551,000
	$465,646,000	$451,980,000
Total revenues	$ 35,180,000	$ 34,289,000
Net income	$ 3,927,000	$ 4,608,000

Wesco's appropriated retained earnings at December 31, 1974 and 1973 include approximately $43,852,000 and $43,256,000, respectively of tax reserves for which no provision for federal income taxes has been made. If in the future these appropriations are used for any purpose other than to absorb bad debt losses, federal income taxes will be imposed at the then applicable rates. The Federal Savings and Loan Insurance Corporation, in connection with the insurance of savings deposits, requires savings and loan associations to maintain certain reserves which may be used only for the purpose of absorbing losses. In addition, associations must maintain certain reserves under California law. Such reserve requirements were met as of December 31, 1974 and 1973.

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 estimates of the cost of merchandise and related redemption expenses. The Company's estimated cost of future redemptions depends on two factors: (1) the percentage of stamps issued which will ultimately be redeemed and (2) the future cost of the merchandise and redemption expenses per stamp which will be required. The Company's accounting practice for many years has been to assume that 97.5% of stamps issued will ultimately be redeemed and to base its estimate of future redemption costs per stamp on the most recent information available. Both assumptions are considered less reliable now than in previous years because of the substantial decline in the Company's issuances of trading stamps and continuing increases in total redemption costs per stamp. Under such conditions, the current redemption rate may well be less than the 97.5% estimated with respect to prior years, and future redemption costs per stamp may well be higher than those projected. Because the Company does not yet have sufficient experience to be reasonably certain of a revised redemption rate or of the appropriateness of revising its method of estimating the future cost of merchandise and related redemption expenses, the Company has continued use of its historical accounting practice. The liability for unredeemed trading stamps of $72,183,000 at March 1, 1975, included $55,581,000 for the cost of merchandise and $16,602,000 for redemption expenses.

NOTE 3 — Marketable securities:

Following is a summary of marketable securities, which are stated at cost determined by the first-in, first-out method:

	Cost	Market Value
March 1, 1975—		
Short-term investments	$ 5,382,000	$ 5,382,000
Preferred and common stocks ..	72,159,000	54,212,000
	$ 77,541,000	$ 59,594,000
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

Marketable securities, among other assets, are held primarily for the purpose of satisfying the Company's obligation to redeem outstanding trading stamps which, based on the Company's experience, will be presented for redemption over a number of years.

NOTE 4 — Property, fixtures and equipment:

Following is a summary of property, fixtures and equipment, stated at cost:

	March 1, 1975	March 2, 1974
Land	$ 2,323,000	$ 2,900,000
Buildings	4,031,000	5,755,000
Furniture, fixtures and equipment	9,047,000	9,289,000
Leasehold improvements.	4,465,000	4,287,000
	19,866,000	22,231,000
Less accumulated depreciation and amortization	11,593,000	11,777,000
	$ 8,273,000	$10,454,000

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 $1,220,000 and $1,353,000 for the fiscal years ended in 1975 and 1974.

A $1,254,000 gain on the sale of the Company's Richmond, California warehouse is included in other revenues in the fiscal year ended in 1975.

NOTE 5 — Debentures:

The indenture underlying the debentures requires three annual sinking fund payments of $2,168,000 on approximately November 30, 1976 through 1978. During the fiscal year ended in 1975 the Company purchased and retired $4,041,000 principal amount of debentures in anticipation of its November 30, 1974 and 1975 sinking fund requirements. Gains of $311,000 resulting from the purchases are included in other revenues.

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 net income for the preceding fiscal year. Dividends may not be paid if the Company is in arrears in any sinking fund payments.

NOTE 6 — Pension and profit sharing plans:

Employees of the Company and of its consolidated subsidiary who meet certain eligibility requirements are covered under either Company-sponsored non-contributory pension or profit sharing plans or union-sponsored pension plans. The Company-sponsored plans are funded annually; the cost for the fiscal years ended in 1975 and 1974 approximated $386,000 and $435,000 respectively. There are no unfunded vested benefits under the plans.

The Employee Retirement Income Security Act of 1974 is principally concerned with participation, vesting, and funding requirements. The Company does not expect that amendments to the pension and profit sharing plans which may be required under the Act will have a significant financial impact.

NOTE 7 — Taxes on income:

The consolidated statement of income contains charges for income taxes as follows:

	Fiscal year ended in	
	1975	1974
Provision for income taxes	$1,237,000	$2,071,000
Charged against equity in net income of Wesco Financial Corporation .	244,000	32,000
Charged (credited) against securities gains (losses)	284,000	(9,000)
Extraordinary credit, representing federal income tax not payable due to the offset of capital loss carry-forwards ...	(903,000)	—
Total taxes charged in income statement	$ 862,000	$2,094,000

These taxes are payable as follows:

	Fiscal year ended in	
	1975	1974
Payable currently—		
Federal	$ 788,000	$1,440,000
State	789,000	667,000
	1,577,000	2,107,000
Payable (recoverable) in the future—		
Federal	(543,000)	(18,000)
State	(172,000)	5,000
	(715,000)	(13,000)
Total taxes charged in income statement	$ 862,000	$2,094,000

Of the above taxes, the amounts currently payable are included in income taxes payable on the consolidated balance sheet .The amounts payable (recoverable) in the future are included in prepaid income taxes or income taxes payable and result from the following timing differences in the recognition of revenue and expense items on the books as compared to the tax returns:

	Fiscal year ended in 1975	1974
Deductible California franchise taxes over (under) those accrued on the books	$ 429,000	$ (70,000)
Deductible redemption expenses over (under) those accrued on the books	(1,351,000)	57,000
Deferred taxes on undistributed earnings of Wesco Financial Corporation	113,000	—
Other timing differences	94,000	—
Total taxes recoverable in the future	$ (715,000)	$ (13,000)

The consolidated balance sheet includes prepaid income taxes of $4,925,000 and $3,815,000 at March 1, 1975 and March 2, 1974, resulting primarily from deducting certain redemption expenses for tax purposes when stamps are redeemed and for book purposes when stamps are issued.

The provision for income taxes of $1,237,000 for the fiscal year ended in 1975 amounted to 18.7% of pre-tax income of $6,614,000; the provision of $2,071,000 for the prior fiscal year represented 23.4% of pre-tax income of $8,838,000. Following is a summary of the differences between the federal statutory rate and these effective percentages:

	Fiscal year ended in 1975	1974
Statutory federal income tax rate	48.0%	48.0%
Federal tax benefit from dividend exclusion	(31.5)	(27.7)
State income taxes net of federal income tax benefit	5.1	3.8
All other (net)	(2.9)	(.7)
Effective income tax rate	18.7%	23.4%

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

The Internal Revenue Service has examined federal income tax returns for the fiscal years ended in 1969 through 1974. As a result of the examination for the three fiscal years ended in 1971, the Service proposed a tax deficiency of approximately $5,500,000, excluding interest. The proposed deficiency 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 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. The California Franchise Tax Board proposed assessment of additional taxes based on the federal notice, and the Company filed a protest. The Company has not received a revenue agent's report for the three fiscal years ended in 1974 but expects substantial additional deficiencies to be proposed. Payment of additional taxes and interest, if any, for all open years, together with any related accounting adjustments, is not expected to have a material adverse or favorable effect upon stockholders' equity.

NOTE 8 — Stock options:

Under the Company's qualified stock option plan, options to purchase 18,700 shares of the Company's common stock were outstanding at March 1, 1975 (of which 12,950 were currently exercisable) at approximately $15.00 per share. No options were granted or exercised during the fiscal year.

NOTE 9 — Lease commitments and rental expense:

At March 1, 1975 minimum rental commitments are as follows:

Fiscal year ending in—	
1976	$2,659,000
1977	2,352,000
1978	1,987,000
1979	1,800,000
1980	1,635,000
Five fiscal years ending in—	
1985	3,017,000
1990	805,000
1995	114,000

Net rental expenses were $4,070,000 and $3,708,000 for the fiscal years ended in 1975 and 1974. Rentals applicable to candy operations are generally determined on the basis of a fixed percentage of sales subject to a specific minimum rental. Percentage rental expenses in excess of minimum rentals, which are included above, were $1,288,000 and $913,000 for the fiscal years ended in 1975 and 1974.

Substantially all of the candy subsidiary's leases are, based on current assumptions, considered "financing leases" as defined by the Securities and Exchange Commission. The respective present values of aggregate rental commitments (including estimated future percentage rentals) of these leases were approximately $11,315,000 and $10,735,000 at March 1, 1975 and March 2, 1974. In computing present values, prime interest rates ranging from 1.5% to 12% were used and averaged approximately 6% in each of the fiscal years. The effect on net income, assuming the leases had been capitalized at inception, would not have been material.

NOTE 10 — Legal proceedings:

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 it to discontinue issuance of trading stamps. However, the Company now considers forced consummation of any sale or spin-off unlikely.

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 class action complaint against the Company 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. The class action complaint was also amended effective September 19, 1974 to assert, in substance, that the Company's predecessor had engaged in similar conduct from 1961 until its merger into the Company in 1968, and that the Company must respond in respect of the alleged liability of its predecessor to plaintiffs and the persons they purport to represent for over-reimbursement of sales taxes. 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 as amended is estimated at $17,000,000 less the amount of any money which may be recovered on the claims against the state. Counsel believes the prospects for some 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 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 stockholders. On petition of the Company, the United States Supreme Court granted review and on March 24, 1975 the case was argued and submitted for decision to the Supreme Court. On June 5, 1974 the Company was served with a complaint in a substantially identical action filed in Los Angeles County Superior Court on June 21, 1971. Further proceedings have been held in abeyance in this state action by mutual consent until determination by the United States Supreme Court in the federal 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.

Directors and Officers

DIRECTORS

Warren E. Buffett
Personal investments; Chairman of the Board of Berkshire Hathaway Inc., which is engaged in insurance, textiles and banking, and of Diversified Retailing Company, Inc., which is engaged in the operation of women's apparel stores

Z. Wayne Griffin
Personal investments; real estate development

John P. Guerin, Jr.
General partner of J. P. Guerin & Co., investors

Joseph P. Hughes
Chairman of the Board of Hughes Markets, Inc., a retail grocery chain; a director of Certified Grocers of California, Ltd., a wholesale grocery cooperative

Emmett H. Jones
President of Terminal Oil Company, an oil exploration and producing company, Industrial Engineering & Equipment Corporation, a seller of electrical equipment, and Westates Investment Co., an investment company

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., a retail grocery chain

OFFICERS

Donald A. Koeppel
Chairman of the Board and President

William F. Ramsey
Executive Vice President

Raymond H. Allen
Vice President, Information Systems

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

Stock Quotations

The following table summarizes the range of over-the-counter quotations reported by the National Association of Securities Dealers, Inc. with respect to the Company's common stock:

	High		Low	
Fiscal Quarter Ended	Bid	Asked	Bid	Asked
June 2, 1973	14⅝	15⅛	10	10¾
September 1, 1973	10	10½	7¾	8½
December 1, 1973	11	11¾	8¼	9
March 2, 1974	8¾	9½	7¼	8
June 1, 1974	8¼	9	6¾	7½
August 31, 1974	7½	8¼	5½	6¼
November 30, 1974	7	7¾	5½	6¼
March 1, 1975	7¼	8	4¾	5½

A cash dividend of $.06 per share was paid in each quarter.

WESCO FINANCIAL CORPORATION

Annual report 1974

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Headquarters building of Wesco Financial Corporation and Mutual Savings -- Pasadena's City Hall in foreground

MUTUAL SAVINGS AND LOAN ASSOCIATION **PASADENA**

Head Office: 315 EAST COLORADO BOULEVARD • PASADENA, CALIFORNIA • 91109

Branches: Glendale, Covina, West Arcadia, Corona del Mar, Canoga Park, Thousand Oaks, Capistrano-San Clemente, Vista, Santa Ana, Channel Islands, Fountain Valley and Lake San Marcos, California

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TO THE STOCKHOLDERS OF WESCO FINANCIAL CORPORATION

Consolidated net earnings after taxes of Wesco Financial Corporation and its subsidiaries for 1974 amounted to $3,927,000 ($1.65 per share) compared to $4,608,000 ($1.94 per share) in 1973. Quarterly earnings per share for 1974 and 1973 were:

	1974	1973
First quarter	$ .48	.60
Second quarter	.40	.47
Third quarter	.44	.47
Fourth quarter	.33	.40
Year	$1.65	1.94

The reduction in net income for the fourth quarter is principally caused by a reduction in loans made and losses taken on sale of marketable securities. Loans made during the fourth quarter were $4,466,000 compared with $27,360,000 made during the first nine months of the year. Total losses on securities amounted to $429,000 for the year of which $350,000 were sustained in the fourth quarter. These fourth quarter losses were taken to improve the quality and yield of securities held. If such fourth quarter securities losses had not been taken, earnings for that quarter would have been $.40 per share.

A "Summary of Operations" for a five-year period is presented on page 3, followed by "Management's Discussion and Analysis" of that Summary. The purpose of the Summary and Discussion is to enable investors to compare periodic results of operations and to assess the source and probability of earnings.

Total savings in Mutual Savings decreased $12,413,000 in 1974 compared with a decrease of $15,742,000 in 1973. Out-of-state savings decreased $16,257,000, and local savings increased $3,844,000 in 1974. In 1973, out-of-state savings decreased $13,694,000 and local savings decreased $2,048,000. At December 31, 1974 out-of-state savings totalled $57,574,000 (17.3% of savings) compared with $73,831,000 (21.3% of savings) at December 31, 1973.

On July 1, 1973, the Federal Home Loan Bank authorized higher interest rates on savings accounts, which had a significant effect on the cost of savings. The highest rate authorized was 7½% for certificates maturing in four years or more. Effective December 23, 1974 another type certificate was authorized providing for a rate of 7¾% for a term of six years or more. As a result of these interest rate changes, substantial funds are being converted from maturing lower-rate certificates to those bearing an interest rate of 7½% or 7¾%. There is no rate limit on certificates of $100,000 or more. Savings accounts at December 31 by interest rates paid are summarized:

	1974	1973	1972
5 %	—%	—	38
5¼	36	35	5
5½	2	3	3
5¾	3	6	4
6	23	42	48
6½	8	5	2
6¾	3	1	—
7	1	1	—
7½	22	7	—
9	1	—	—
10	1	—	—
	100%	100	100

The recent decline in short-term interest rates has resulted in resumption of overall savings growth. We continue to experience losses in out-of-state savings. Substantial savings growth should be experienced for in-state savings during the first half of 1975, and may continue through the entire year. None of the basic problems of the American economy have been solved. The economy continues to suffer from both high inflation and deepening recession. Until further time elapses and Government programs are adopted and can be evaluated, the outlook in 1975 for the savings and loan industry is uncertain. Our present intent is to restrict lending so as to increase liquidity substantially, and thereafter to reduce bank indebtedness which at December 31, 1974 was $50,975,000.

The cost of savings for 1974 was 6.00% compared with 5.60% for 1973. Cost of all funds (savings and borrowings), which was 5.69% for 1973, increased to 6.25% for 1974. The interest rate on borrowings is expected to decrease moderately during 1975, but we believe that the interest rate required to be paid for savings will increase in 1975.

The interest rate on the loan portfolio, which was 7.17% at December 31, 1973, increased to 7.36% at December 31, 1974. The rate of increase in yield on the loan portfolio may moderate somewhat in 1975 because of limited lending volume and an

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expected decrease in the rate of interest that can be charged on new loans.

The following illustrates the increase in cost of savings, cost of all funds and yield on loans:

	1970	1971	1972	1973	1974
Cost of Savings	5.39%	5.51	5.56	5.60	6.00
Cost of all Funds	5.91	5.71	5.59	5.69	6.25
Yield on Loans at year end	6.71	6.82	7.03	7.17	7.36

Real estate loans made during 1974 totalled $31,998,000 compared with $52,647,000 in 1973. Loans in process and firm loan commitments, which at December 31, 1973 were $22,185,000, have decreased to $3,240,000 at December 31, 1974.

The increase of $506,000 in general and administrative expenses from $3,702,000 (10.8% of gross income) in 1973 to $4,208,000 (12.0% of gross income) in 1974 was caused by inflation, the expense of opening and operating additional branch offices and the cost of computerizing our accounting system.

In 1973 Mutual Savings disposed of 17 residential units which it had previously constructed in the Friendly Valley development. During 1974, Mutual completed 143 units at that location. As of December 31, 1974, 70 units had been sold, with 45 of the sales recorded and 25 in escrow. In January, 1975 an additional 9 units were sold. It is expected that the remaining 64 units will be disposed of during 1975. Construction of 58 additional units may be commenced during 1975. Mutual Savings had planned to construct during 1974 82 units on real property in Glendora, California. The property was sold in January, 1975 to a responsible builder who is presently constructing 80 residential units on this property. Upon the disposition of the units, which we expect to occur during 1975, we will report a profit of $192,000 as a gain on sale of this land.

Mutual Savings has substantial amounts of vacant land remaining at the Friendly Valley development, at Lake San Marcos in San Diego County and at Montecito in Santa Barbara County. Sales are in negotiation for portions of the San Marcos property. Disposition of additional property at Friendly Valley and in Santa Barbara will have to await economic recovery.

In April, 1974 the California Savings and Loan Commissioner adopted certain regulations authorized by legislation enacted in 1973, which gave to California savings and loan associations authority to invest 2% of assets in commercial paper, 2% of assets in non-convertible corporate debt securities, and 5% of assets in preferred stock of public utilities corporations. Mutual Savings and Wesco have purchased public utilities preferred stocks, and as of December 31, 1974 had invested $12,900,000 ($7,150,000 in California corporations) in such stocks with an annual yield of 9.77%. At December 31, 1974, Wesco owned 200,900 shares of Crocker National Corporation (a California corporation), purchased in 1973 at a cost of $5,079,000. Based on current dividends of $1.66 per share, the annual yield is 6.57%, 85% of dividend income is deductible in computing our Federal Income Taxes. For California Franchise Tax purposes, all dividend income of the California public utilities is deductible and approximately 90% of the dividend of Crocker National Corporation is deductible.

During 1974 Mutual opened branch offices in Santa Ana, Oxnard, Fountain Valley and Lake San Marcos. Three new branch offices were opened in 1973. Approval has been received for branch offices at Upland and Cerritos, which will commence operation during the second quarter of 1975, bringing the number of Mutual Savings offices to 15.

On January 21, 1975 Wesco increased its regular quarterly cash dividend from 10¢ to 15¢ per share, with the first 15¢ quarterly dividend payable March 13, 1975 to holders of record at the close of business on February 18, 1975. In 1974 50¢ was paid consisting of four regular dividends and an extra dividend each of 10¢ per share. No extra dividend is contemplated during 1975.

Blue Chip Stamps made two tender offers during 1974, one of which expired on April 15 and the other on September 6. Blue Chip Stamps now owns approximately 64.4% of Wesco's outstanding stock, as compared with 44.6% on December 31, 1973.

Louis R. Vincenti

LOUIS R. VINCENTI
Chairman of the Board and President

WESCO FINANCIAL CORPORATION AND SUBSIDIARIES

Summary of Operations

Year ended December 31, 1974 and four prior years

	1974	1973	1972	1971	1970
Investment income:					
Interest on loans	$ 28,463,000	27,450,000	25,318,000	25,117,000	25,866,000
Interest on marketable securities	3,202,000	2,950,000	2,362,000	1,740,000	1,418,000
Dividends on common and preferred stocks	974,000	463,000	185,000	—	—
Interest and dividends on investments required by law	533,000	462,000	251,000	388,000	469,000
Total investment income	33,172,000	31,325,000	28,116,000	27,245,000	27,753,000
Cost of money:					
Interest on savings deposits	20,419,000	20,001,000	19,304,000	17,298,000	15,283,000
Interest on notes payable	3,364,000	1,313,000	611,000	3,105,000	6,965,000
Total cost of money	23,783,000	21,314,000	19,915,000	20,403,000	22,248,000
Margin on investments	9,389,000	10,011,000	8,201,000	6,842,000	5,505,000
Loan fees and service charges	1,542,000	1,786,000	2,662,000	1,684,000	1,169,000
Operations and net gains from sales of real property	593,000	831,000	622,000	320,000	1,166,000
Rental of office premises, net	206,000	303,000	261,000	238,000	312,000
Net gains or (losses) on sales of marketable securities	(429,000)	(72,000)	2,000	51,000	(69,000)
Other income, net	96,000	116,000	124,000	111,000	102,000
	11,397,000	12,975,000	11,872,000	9,246,000	8,185,000
General and administrative expenses	4,208,000	3,702,000	3,436,000	3,127,000	3,105,000
Earnings before taxes on income	7,189,000	9,273,000	8,436,000	6,119,000	5,080,000
Taxes on income:					
Current	3,262,000	4,263,000	3,018,000	2,530,000	994,000
Deferred	—	402,000	1,082,000	465,000	1,037,000
	3,262,000	4,665,000	4,100,000	2,995,000	2,031,000
Net earnings	$ 3,927,000	4,608,000	4,336,000	3,124,000	3,049,000
Per share*	$ 1.65	1.94	1.83	1.32	1.28
FINANCIAL DATA AT YEAR END					
Total assets	$465,646,000	451,980,000	448,240,000	423,969,000	434,445,000
Real estate loans	$336,398,000	387,165,000	367,679,000	356,933,000	375,593,000
Savings accounts	$333,117,000	345,530,000	361,272,000	329,782,000	288,652,000
Shareholders' equity	$ 70,291,000	67,551,000	64,018,000	59,682,000	56,558,000
Book value per share*	$ 29.62	28.46	26.98	25.15	23.83

*Per share earnings and book value per share are based on 2,373,269 shares outstanding at December 31, 1974.

Management's Discussion and Analysis of Summary of Operations

The accompanying Summary of Operations covers the five years ended December 31, 1974.

The principal business of Wesco Financial Corporation (Wesco) is the ownership of all of the outstanding stock of Mutual Savings and Loan Association, which operates in Southern California through thirteen offices located in Los Angeles, Orange, Ventura and San Diego Counties. Wesco also owns and operates a Pasadena business block in which its head office and the head office of Mutual Savings are located. This block is fully improved with a 9-story modern office building, a 420-car garage and four retail stores. Wesco invests its cash funds in marketable securities and at December 31, 1974 had so invested the sum of $12,799,000. Mutual Savings' principal business is the lending of money secured by first liens on real estate (principally residential) to enable borrowers to purchase, construct or refinance real property. Funds are provided by savings deposits, principal payments on existing loans, borrowings from banks and operations.

INTEREST ON LOANS. This source of income is dependent upon the amount of loans and the yield thereon. The yields at December 31, 1972, 1973 and 1974 were 7.03%, 7.17% and 7.36% respectively. Total real estate loans outstanding at the end of said years were $367,679,000, $387,165,000 and $386,398,000.

INTEREST ON MARKETABLE SECURITIES. Investments have consisted principally of certificates of deposit of major banks, bankers acceptances, United States Government bonds, notes, bills and agency securities. The variation in income shown on the accompanying Summary is accounted for by the varying amounts invested and the varying yields obtained in the particular year. The amount invested in marketable securities from time to time is dependent on the cash flow available for investment and the amount committed for investment in real estate loans.

DIVIDENDS ON COMMON AND PREFERRED STOCKS. No common or preferred stocks were owned in 1971 and prior years. During 1972 Wesco invested $4,102,000 in public utility preferred stocks, which during that year produced an income of $201,000. These stocks were disposed of during the first quarter of 1973. In May, 1973 $6,785,000 was invested in the common stock of Crocker National Corporation. A portion of the stock was sold in early 1974, and the investment at December 31, 1974 was $5,079,000. At December 31, 1974 Wesco and Mutual Savings had invested $12,900,000 ($267,000 by Wesco) in public utility preferred stocks. The income reflected in the accompanying Summary is that earned in the particular year from the securities purchased and held as indicated. 1975 dividend income on the investment of $13,927,000 in preferred stocks now owned is projected to be $1,369,000 as compared with $611,000 on preferred stocks in 1974. If the dividend rate of $1.66 per share is maintained, dividends on Crocker stock, which amounted to $363,000 in 1974, will be $333,000 in 1975. At 1974 year end the market value of the common and preferred stocks was below the investment, but since that date the market value of the portfolio has increased substantially. We believe that the market decline of the common stock is a temporary condition and that no permanent loss will be sustained. The market value of preferred stocks varies as interest rates vary. Since interest rates at year end were higher than rates at the time of purchase, the market value of our preferred stocks was below cost. Interest rates have since declined, with the result that the market value of our preferred stocks is now substantially above cost. The investments in common and preferred stocks and their market values for Wesco consolidated are summarized as follows:

	December 31, 1974		February 28, 1975	
	Investment Cost	Market Value	Investment Cost	Market Value
Common stock	$ 5,079,000	3,039,000	5,079,000	3,968,000
Preferred stocks	12,900,000	11,831,000	13,927,000	14,431,000

INTEREST AND DIVIDENDS ON INVESTMENTS REQUIRED BY LAW. This source of income consists of dividends received on stock of the Federal Home Loan Bank of San Francisco and interest received on our secondary reserve held by the Federal Savings and Loan Insurance Corporation. No dividend was paid in 1972, $189,000 was paid in 1973 and $229,000 in 1974. The variation in amount of interest on the secondary reserve has been nominal.

INTEREST ON SAVINGS DEPOSITS. Savings at December 31, 1971 totalled $329,782,000, increased to $361,272,000 by 1972 year end, then decreased to $345,530,000 at the end of 1973 and to $333,117,000 at the end of 1974. The increase of interest paid on savings deposits in 1973 over 1972 was caused by a substantial increase in rates paid on savings accounts effective July 1, 1973. Although savings declined further during 1974, interest paid on savings deposits increased due to higher rates continuing through the entire year of 1974 and due to substantial funds being converted from maturing lower-rate certificates to certificates bearing interest rates of 7½% or 7¾%.

INTEREST ON NOTES PAYABLE. The variation in interest on notes payable is due to fluctuations in amounts borrowed from time to time and varying rates paid thereon. During 1972 rates of interest on borrowings varied from 6⅞% to 8⅛%, in 1973 from 7½% to 9¾% and in 1974 from 7½% to 12%.

MARGIN ON INVESTMENTS. Margin on investments is the difference between total investment income and the cost of money, and is made up of the items discussed above. The $1,810,000 increase of margin in 1973 over 1972 is the result of an increase of investment income of $3,209,000 less an increase in the cost of money of $1,399,000. In 1974, while investment income increased $1,847,000, cost of money increased by $2,469,000 resulting in a $622,000 decrease of the margin on investments.

LOAN FEES AND SERVICE CHARGES. This income was derived from the following sources:

	1972	1973	1974
Loan fees	$1,410,000	855,000	858,000
Commitment fees	416,000	180,000	89,000
Escrow and clerical fees	125,000	139,000	102,000
Prepayment charges	415,000	341,000	334,000
Late charges	159,000	152,000	59,000
Other charges	137,000	119,000	100,000
	$2,662,000	1,786,000	1,542,000

Reduction in loans and commitments for loans, and in fees charged for such loans and commitments, account for most of the annual reduction in the total income from this source.

OPERATIONS AND NET GAINS FROM SALES OF REAL PROPERTY. Mutual Savings, over a period of years, has acquired foreclosed real property including vacant land. Some vacant land has been disposed of from time to time and, on other occasions, residential units were built thereon and sold. Mutual Savings has also acquired foreclosed residential properties and disposed of them. During 1972 Mutual Savings sold 118 residential units of which 92 units had been constructed by it, in 1973 sold 38 residential units of which 17 had been constructed by it, and in 1974 sold 53 units of which 45 had been constructed by it. In 1972 no significant profit or loss was sustained on the sale of vacant land. In 1973 a parcel of vacant land was sold in Santa Barbara County resulting in a profit of $495,000, and in 1974 a parcel of land was sold in San Diego County resulting in a profit of $215,000. The variation in sale of residences and of vacant land accounts for the variation in the income shown on the accompanying Summary.

RENTAL OF OFFICE PREMISES, NET. Substantially all of this income is derived from the Pasadena business block owned by Wesco in which the head office of Mutual Savings is located. The variation in income from 1972 to 1973 is substantially accounted for by additional percentage rents received from tenants of two commercial stores. The decrease from $303,000 in 1973 to $206,000 in 1974 is attributable to a $32,000 increase in expenses and the loss, at December 31, 1973, of a tenant occupying 26,000 square feet of space (20% of total rentable space). By December 31, 1974 16,000 square feet of that space had been leased. At 1974 year end 9,800 square feet of space was vacant. Rents are being increased as the leases expire, and some improvement of rental income in 1975 can be expected over that of 1973.

NET GAINS (LOSSES) ON SALES OF MARKETABLE SECURITIES. A loss of $429,000 taken on sale of securities in 1974 is accounted for by two transactions. In order to improve the quality and yield on public utility preferred stocks owned, some sales were made at a loss of $171,000 and the funds reinvested in other preferred stocks considered of better quality and providing a higher yield. Government and agency obligations were sold at a loss of $256,000 and proceeds reinvested so as to reduce the time to maturity.

GENERAL AND ADMINISTRATIVE EXPENSES. The increase of $266,000 from 1972 to 1973 was occasioned principally by the expense of opening and operating three additional branch offices during 1973. Operating expenses in 1972 were 10.8% of gross income. The $506,000 increase in general and administrative expense from $3,702,000 (10.8% of gross income) in 1973 to $4,208,000 (12% of gross income) in 1974 was occasioned by inflation, the expense of opening and operating four additional offices in 1974, and the cost of computerizing our accounting system.

TAXES ON INCOME. Taxes on income were 48.6% of earnings before taxes on income in 1972, 50.3% in 1973 and 45.4% in 1974. Total tax expense varies with the increase or decrease in pre-tax accounting income adjusted for permanent differences (generally non-taxable revenue or non-deductible expense items). In 1972 the permanent differences and the increases (or reductions) in taxes were as follows:

Net gains on sales of foreclosed real property	($357,000)
State franchise tax net of Federal income tax benefit	$467,000
Dividends received deduction on preferred stocks	($ 75,000)
Other permanent differences	$ 16,000

Note 4 of the notes to the consolidated financial statements describes the permanent differences for 1973 and 1974 and their tax effects. Deferred tax expense was $1,082,000 in 1972, $402,000 in 1973 and was nil in 1974. The decrease in deferred taxes was caused principally by the decrease in loan fees recognized for financial statement purposes and the increase in loan fees recognized for tax purposes.

STOCK MARKET DATA. The following table indicates the quarterly high and low prices for Wesco's capital stock on the New York Stock Exchange for the last two years:

1973			1974	
High	Low	Quarter Ended	High	Low
18¼	14¾	March 31	15	11⅛
16¼	11⅛	June 30	15	9⅝
13⅜	10½	September 30	13½	6¼
14⅞	10¼	December 31	9¼	7½

Consolidated Balance Sheets

December 31, 1974 and 1973

ASSETS	1974	1973
Cash	$ 1,067,000	1,151,000
Marketable securities (note 3):		
Certificates of deposit	24,010,000	21,998,000
United States Government and agency obligations and other marketable securities, at amortized identified cost (quoted market, $9,953,000 in 1974 and $10,056,000 in 1973)	10,009,000	10,178,000
Investment in common stocks (quoted market, $3,039,000 in 1974 and $5,996,000 in 1973)	5,079,000	6,785,000
Investment in preferred stocks (quoted market, $11,831,000 in 1974)	12,900,000	—
Loans receivable, less unearned loan fees, unrealized profit and loans in process (notes 2 and 3)	389,065,000	389,584,000
Accrued interest and dividends receivable	1,935,000	1,960,000
Properties purchased and held for investment, at cost	661,000	455,000
Properties acquired through foreclosure by Mutual Savings and held for sale, at cost less allowance for losses, $280,000 in 1974 and 1973 (note 3)	5,819,000	5,451,000
Investments required by law:		
Investment in stock of Federal Home Loan Bank, at cost (note 3)	3,745,000	3,691,000
Prepayments to FSLIC secondary reserve	4,863,000	4,644,000
Office properties and equipment, net (note 5)	5,140,000	5,297,000
Prepaid expenses and sundry assets, at cost	1,353,000	786,000
	$465,646,000	451,980,000

LIABILITIES AND STOCKHOLDERS' EQUITY		
Cash disbursements to be funded at bank	$ 1,248,000	—
Savings deposits	333,117,000	345,530,000
Notes payable (note 3)	50,975,000	27,705,000
Advances by borrowers for taxes and insurance	1,129,000	1,261,000
Accounts payable and sundry accrued expenses	996,000	1,101,000
Taxes on income (note 4):		
Current	41,000	983,000
Deferred	7,849,000	7,849,000
Total liabilities	395,355,000	384,429,000
Stockholders' equity (notes 4, 7 and 8):		
Capital stock of $1 par value per share. Authorized 2,500,000 shares; issued 2,373,269 shares	2,373,000	2,373,000
Capital surplus arising from stock dividends	28,066,000	28,066,000
Retained earnings	39,852,000	37,112,000
Total stockholders' equity	70,291,000	67,551,000
Commitment and contingent liabilities (notes 6 and 10).		
	$465,646,000	451,980,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Earnings

Years ended December 31, 1974 and 1973

Investment income:		
Interest on loans	$ 28,463,000	27,450,000
Interest on marketable securities	3,202,000	2,950,000
Dividends on common and preferred stocks	974,000	463,000
Interest and dividends on investments required by law	533,000	462,000
Total investment income	33,172,000	31,325,000
Cost of money:		
Interest on savings deposits	20,419,000	20,001,000
Interest on notes payable	3,364,000	1,313,000
Total cost of money	23,783,000	21,314,000
Margin on investments	9,389,000	10,011,000
Loan fees and service charges	1,542,000	1,786,000
Operations and net gains from sales of real property (note 9)	593,000	831,000
Rental of office premises, net	206,000	303,000
Net losses on sales of marketable securities	(429,000)	(72,000)
Other income, net	96,000	116,000
	11,397,000	12,975,000
General and administrative expenses	4,208,000	3,702,000
Earnings before taxes on income	7,189,000	9,273,000
Taxes on income (note 4):		
Current	3,262,000	4,263,000
Deferred	—	402,000
	3,262,000	4,665,000
Net earnings	$ 3,927,000	4,608,000
Earnings per capital share based on 2,373,269 shares	$ 1.65	1.94

See accompanying notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity

Years ended December 31, 1974 and 1973

	1974	1973
Capital stock (note 7):		
Beginning of year	$ 2,373,000	2,260,000
5% stock dividend	—	113,000
End of year	2,373,000	2,373,000
Capital surplus arising from stock dividends (note 7):		
Beginning of year	28,066,000	26,399,000
Excess of market value of stock dividend over par value of stock issued	—	1,667,000
End of year	28,066,000	28,066,000
Retained earnings:		
Appropriated (notes 4 and 8):		
Beginning of year	42,446,000	41,587,000
Allocation of net earnings	596,000	859,000
End of year	43,042,000	42,446,000
Unappropriated (note 7):		
Beginning of year	23,905,000	21,231,000
Cash dividends declared and paid	(1,187,000)	(1,075,000)
Allocation of net earnings	3,331,000	3,749,000
End of year	26,049,000	23,905,000
Less stock dividends at market value (note 7):		
Beginning of year	(29,239,000)	(27,459,000)
Market value of stock dividend	—	(1,780,000)
End of year	(29,239,000)	(29,239,000)
Total retained earnings	39,852,000	37,112,000
Total stockholders' equity	$ 70,291,000	67,551,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Financial Position

Years ended December 31, 1974 and 1973

	1974	1973
Funds provided:		
Net earnings	$ 3,927,000	4,608,000
Charges (credits) to earnings not requiring (providing) funds:		
Depreciation and amortization	314,000	294,000
Interest on savings deposits credited to savings accounts	14,810,000	14,005,000
Deferred income taxes (note 4)	—	402,000
FSLIC primary premium transferred from secondary reserve	86,000	91,000
Amortization of fees and discounts	(409,000)	(402,000)
Recognition of unrealized profit on real property	(410,000)	(259,000)
Interest income on FSLIC secondary reserve	(305,000)	(273,000)
Funds provided from operations	18,013,000	18,466,000
Principal payments on real estate loans	35,029,000	44,326,000
Additions to deferred loan fees	277,000	329,000
Sales of real property, net of gains	1,769,000	2,804,000
Increase in notes payable	23,270,000	14,985,000
Increase in advances by borrowers for taxes and insurance	—	349,000
Additions to unrealized profit on real property	155,000	340,000
Decrease in marketable securities	—	15,931,000
Decrease in cash	1,332,000	430,000
Total funds provided	$ 79,845,000	97,960,000
Funds used:		
Cash dividends declared and paid (note 7)	$ 1,187,000	1,075,000
Decrease in savings deposits	27,223,000	29,747,000
Investment in real estate loans	31,998,000	52,647,000
Investment in buildings and other assets	282,000	228,000
Additions to real property	2,219,000	1,716,000
Decrease in loans in process	1,883,000	11,173,000
Investment in stock of Federal Home Loan Bank	54,000	—
Decrease in advances by borrowers for taxes and insurance	132,000	—
Increase in marketable securities	13,037,000	—
Other, net	1,830,000	1,374,000
Total funds used	$ 79,845,000	97,960,000

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements
December 31, 1974 and 1973

(1) Summary of Significant Accounting Policies

The following items comprise the significant accounting policies which the Company follows:

Principles of Consolidation

The consolidated financial statements include the accounts of Wesco Financial Corporation (the Company) and its wholly owned subsidiary, Mutual Savings and Loan Association and its wholly owned subsidiaries (Mutual Savings). All material intercompany transactions have been eliminated.

Marketable Securities

U.S. Government, agency obligations and other marketable securities are carried at identified cost, adjusted for amortization of premium and accretion of discount over the term of the security and are not carried at the lower of cost or market because it is management's intention to hold them to maturity.

Common and preferred stocks are carried at identified cost.

Loan Fees

Loan fees for originating loans are deferred for amounts in excess of 1% of the loan amount plus $200 for non-construction loans and 2% of the loan amount plus $200 for construction loans. Deferred fees are amortized into income by use of the straight-line method over seven years.

Loan Valuation Allowances

Valuation allowances for estimated losses on specific loans are charged to earnings when any significant and permanent decline reduces the market value of the underlying security to less than the loan. Such losses are usually indicated during foreclosure proceedings.

Real Property Valuation Allowances

Valuation allowances for estimated losses on real property are charged to earnings when any significant and permanent decline reduces the market value to less than the carrying value. When the Company intends to hold real estate held for sale for a period in excess of 18 months, future direct holding costs for maintenance, property taxes, insurance, direct selling expenses, costs of completion or improvement and a discount factor to give effect to the cost of money are considered in determining the amount of required valuation allowances.

Office Properties and Equipment

Office properties and equipment are depreciated by use of the straight-line method over the estimated useful lives of the various classes of assets from the respective dates of acquisition. The useful lives used for the principal classes of assets are:

Buildings and improvements	10 to 45 years
Furniture, fixtures and equipment	4 to 10 years
Leasehold improvements	3 to 20 years

Maintenance and repairs are charged to appropriate expense accounts in the year incurred; renewals and material betterments are charged to property accounts.

Cost and accumulated depreciation and amortization applicable to assets retired or otherwise disposed of are eliminated from the related accounts and the profit or loss on disposition is credited or charged to earnings.

Profit on the Sale of Real Property

Profit on the sale of real property is recognized when the buyer has made an irrevocable commitment to the sale and has met certain down payment and amortization requirements. In general, the down payment requirements range from 10% to 25% for improved property and from 15% to 30% for unimproved property based on the use of the property and cash flow projections. Amortization requirements include the payment on an annual level payment basis (principal and interest) over a period not to exceed from 15 to 30 years, depending on the type and use of the property, with payments commencing not later than one year from date of sale.

Comparative Figures

Certain items in the 1973 financial statements have been reclassified to conform with 1974 classifications.

(2) Loans Receivable

Loans receivable are summarized as follows:

	1974	1973
Real estate loans on residential property of:		
One to four units (home loans)	$284,885,000	277,939,000
More than four units	92,786,000	99,864,000
Real estate loans on other properties	11,496,000	14,395,000
	389,167,000	392,198,000
Less:		
Unearned loan fees	(1,075,000)	(1,207,000)
Unrealized profit on sales of real property	(1,404,000)	(1,653,000)
Loans in process	(290,000)	(2,173,000)
	386,398,000	387,165,000
Loans on savings deposits	2,667,000	2,419,000
	$389,065,000	389,584,000

(3) Notes Payable

The following is a summary of notes payable:

Federal Home Loan Bank advances, secured by certain real estate loans and Federal Home Loan Bank stock, with interest from 7.50% to 9.75% in 1974 and 7.50% to 8.125% in 1973, and with maturity dates as follows:

Year ending Dec. 31,	1974	1973
1974	$ —	20,700,000
1975	17,400,000	—
1976	343,000	—
1977	3,494,000	—
1978	3,494,000	—
1979	3,494,000	—
1980	3,494,000	—
1981	3,494,000	—
1982	3,494,000	—
1983	3,494,000	—
1984	1,399,000	—
	43,600,000	20,700,000
Bank notes with interest principally at prime secured by certain marketable securities, real estate loans and real property, and with maturity dates as follows:		
Year ending Dec. 31,		
1974	—	6,085,000
1975	7,375,000	—
Bank note with interest at 9.75% due January 15, 1974, secured by certificate of deposit	—	920,000
	$ 50,975,000	27,705,000

(4) Taxes on Income

If certain conditions are met, savings and loan associations, in determining taxable income, are allowed special bad debt deductions based on specified experience formulas or on a percentage of taxable income before such deduction. The bad debt deduction must be within certain limitations based on outstanding loans and the ratio of reserves, undivided profits and unallocated earnings to savings deposits. Mutual Savings has reached such limitations which preclude deductions from income in arriving at Federal taxes on income.

The investment tax credit, which is insignificant, is recorded by the flow-through method of accounting whereby, in the year available for utilization, it is applied as a reduction of income tax expense.

Appropriated retained earnings at December 31, 1974 and 1973 include approximately $43,852,000 and $43,256,000, respectively (before elimination of $810,000 in consolidation) of tax reserves for which no provision for Federal income taxes has been made. If in the future these appropriations are used for any purpose other than to absorb bad debt losses, Federal income taxes will be imposed at the then applicable rates.

Federal income tax returns of the Company and Mutual Savings for 1972 through 1974 are subject to examination by the United States Treasury Department.

Income tax expense for 1974 and 1973 includes the following components:

	1974		1973	
	Current tax expense	Deferred tax expense	Current tax expense	Deferred tax expense
Federal	$2,451,000	—	3,251,000	251,000
State	811,000	—	1,012,000	151,000
Total	$3,262,000	—	4,263,000	402,000

Deferred tax expense results from timing differences in the recognition of revenue and expense for tax and financial statement purposes. The sources of these differences in 1974 and 1973 and the tax effect of each were as follows:

	1974	1973
Financial statement recognition of loan fees greater (less) than tax recognition	$ (156,000)	577,000
California franchise tax recognized for financial statement purposes on accrual basis but on cash basis for tax purposes	156,000	(125,000)
FSLIC secondary reserve interest income recognized on the financial statements, but deferred for tax purposes	166,000	75,000
Gains on sales of real property recognized in prior years for financial statement purposes	—	(225,000)
Other timing differences ...	(166,000)	100,000
	$ —	402,000

A reconciliation of total income tax expense and the amount computed by applying the U.S. Federal income tax rate of 48% to income before tax follows:

	1974	1973
Computed "expected" Federal tax expense	$ 3,451,000	4,451,000
Increases (reductions) in taxes resulting from:		
Net gains on sales of foreclosed real property	(219,000)	(386,000)
State franchise tax, net of Federal income tax benefit	422,000	606,000
Dividends received deduction on common and pre-preferred stocks	(397,000)	(189,000)
Other permanent differences	5,000	183,000
	$ 3,262,000	4,665,000

(5) Office Properties and Equipment, Net

Office properties and equipment at cost less accumulated depreciation and amortization consist of the following:

	1974	1973
Land	$ 1,509,000	1,62[illegible],000
Office buildings and leasehold improvements	5,780,000	5,659,000
Furniture, fixtures and equipment	930,000	838,000
	8,219,000	8,120,000
Accumulated depreciation and amortization	3,079,000	2,823,000
	$ 5,140,000	5,297,000

(6) Retirement Plan

A noncontributory retirement plan is in effect for all eligible employees of the Company and its subsidiaries. Employer contributions are computed utilizing the aggregate cost funding method. The contributions for 1974 and 1973 approximated $94,000 and $79,000, respectively. The actuarially computed value of vested benefits as of December 31, 1974 and 1973 did not exceed the market value of the assets of the retirement fund.

The Employee Retirement Income Security Act of 1974 became law on September 2, 1974 and is principally concerned with participation, vesting, and funding requirements. Pension plans in existence on January 1, 1974 are not subject to those requirements until plan years beginning after December 31, 1975. Compliance with the requirements of the Act will not have a significant effect on the Company's pension plan.

(7) Dividends

Quarterly cash dividends of $.10 per share plus an extra cash dividend of $.10 per share declared and paid during 1974 amounted to $1,187,000. Cash dividends declared and paid during 1973 amounted to $1,075,000.

On January 16, 1973, the Board of Directors declared a 5% stock dividend (113,013 shares) payable April 3, 1973 to stockholders of record on February 28, 1973. Upon payment of the dividend, the fair market value of the stock ($1,780,000) as of January 16, 1973 was charged to market value of stock dividends, capital stock was credited with an amount equal to the par value of the shares issued ($113,000), and capital surplus was credited with an amount representing the excess of the fair market value over par value ($1,667,000).

(8) Reserve Requirements

The Federal Savings and Loan Insurance Corporation, in connection with the insurance of savings deposits, requires savings and loan associations to maintain certain reserves which may be used only for the purpose of absorbing losses. In addition, associations must maintain certain reserves under California law. Such reserve requirements were met by Mutual Savings as of December 31, 1974 and 1973.

(9) Real Estate Operations

Operations and net gains from sales of real property are summarized as follows:

	1974	1973
Recognized net gains from sales	$ 591,000	852,000
Income from rentals	108,000	140,000
	699,000	992,000
Less maintenance and sales expense	10[illegible]	161,000
	$ 593,000	831,000

(10) Contingent Liabilities

Mutual Savings is named as one of the defendants in several class actions relating to certain common practices in the mortgage lending field. The outcome of this litigation cannot be predicted; however, based on the facts presently available, the Association believes there are substantial defenses to these actions and that losses, if any, would not be material.

In addition, Mutual Savings is a defendant in two actions involving alleged easement rights. Mutual's counsel believes there are meritorious defenses to these actions and there is a substantial chance the cases can be successfully defended. While there is some risk to Mutual, in management's opinion, any such risk would not be material.

Accountants' Report

Peat, Marwick, Mitchell & Co.
CERTIFIED PUBLIC ACCOUNTANTS
[illegible] SOUTH FLOWER STREET
LOS ANGELES, CALIFORNIA [illegible]

The Board of Directors
Wesco Financial Corporation:

We have examined the consolidated balance sheets of Wesco Financial Corporation and subsidiaries as of December 31, 1974 and 1973 and the related consolidated statements of earnings, 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 Wesco Financial Corporation and subsidiaries at December 31, 1974 and 1973 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.

Los Angeles, California
February 14, 1975

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Treasurer

TRANSFER AGENTS AND REGISTRARS

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P.O. Box 3546 Terminal Annex, Los Angeles, California 90051

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4 New York Plaza, New York, New York 10004

LEGAL COUNSEL

Hahn & Hahn

AUDITORS

Peat, Marwick, Mitchell & Co.

LISTED ON

New York Stock Exchange
Pacific Stock Exchange

A copy of Form 10-K for 1974, filed with the Securities and Exchange Commission, is available without charge upon a stockholder's written request addressed to Mrs. Dolores Henderson, Assistant Secretary, Wesco Financial Corporation, 315 East Colorado Boulevard, Pasadena, California 91109.

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END