## Analysis of the 1965 Berkshire Hathaway Shareholder Letter



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## Financial & Valuation Summary

**Financial summary:**

| Fiscal year | Assets | Liabilities | Book value | Sales | % Change sales | Net earnings |
|---|---|---|---|---|---|---|
| 1964 | 27,887,046 | 5,748,293 | 22,138,753 | 49,982,830 | -1.2% | 125,586 |
| 1965 | 28,222,387 | 3,702,273 | 24,520,114 | 49,300,685 | -1.4% | 2,279,206 |

| Fiscal year | (A) Net earnings/Sales | (B) Sales/Assets | (C) Assets/Book value | (A)*(B)*(C) = ROE | Net earnings/BV EOP = ROE | Net earnings/BV BOP = ROE |
|---|---|---|---|---|---|---|
| 1964 | 0.3% | 1.8x | 1.3x | 0.6% | 0.6% | 0.4% |
| 1965 | 4.6% | 1.7x | 1.2x | 9.3% | 9.3% | 10.3% |

**Valuation summary:**

| Fiscal year | Shares outstanding | Book value per share | % Change book value per share | Stock price | % Change stock price | % Change S&P 500 incl. dividends |
|---|---|---|---|---|---|---|
| 1964 | 1,137,778 | $19.46 | 3.3% | $12.37 | NA | NA |
| 1965 | 1,017,547 | $24.10 | 23.8% | $18.50 | 49.5% | 10.0% |

| Fiscal year | P/B | EPS | % Change EPS | P/E | Earnings yield % | Market cap |
|---|---|---|---|---|---|---|
| 1964 | 0.64x | $0.11 | NMF | 112.1x | 0.9% | $14,079,267 |
| 1965 | 0.77x | $2.24 | 1929.3% | 8.3x | 12.1% | $18,824,272 |

## 1965 – The Times They Are a-Changin'[1]

The first annual letter written by Warren Buffett to shareholders was written on November 9, 1965, a few months after Buffett Partnership, Ltd., had taken formal control of Berkshire Hathaway on May 10, 1965.

This changing of the guard in 1965 represented a transformational moment in the long history of Berkshire Hathaway. The year was a monumental fork in the road for the company – a new leader of the enterprise, Warren Buffett, had to decide whether to continue running Berkshire just as it had been run for the past 5 decades or radically deviate from an increasingly untenable, unprofitable status quo. It seems as if Berkshire had also become swept up in the general winds of change and upheaval in 1965 that were fundamentally shaking the very foundation of the United States and the rest of the world. In the grand scheme of things, Berkshire's identity makeover was petty, and such timing was probably mere coincidence.

Regardless, for the sake of providing historical context, it's helpful to take our minds back, to imagine the emotions and thoughts we might have had during this time. The headlines on the front page of *The New York Times* published on Monday, March 8, 1965, shown below, describe some of the wheels that were set in motion in 1965, drastically altering the way we live today.[2]

**"Marines Land to Guard Danang Base"** describes the first U.S. military boots on the ground in Vietnam when 3,500 Marines landed at China Beach on March 8, 1965, to defend the American air base at Da Nang. This event represents a point of no return in the Vietnam War, a dark period in American history. **"Alabama Police Use Gas and Clubs to Rout Negroes"** describes the first Selma to Montgomery march, known as "Bloody Sunday", which helped bring about the passage on August 6, 1965, of the Voting Rights Act of 1965, a quantum leap in civil rights for minorities that legally guaranteed all Americans, regardless of race, the right to vote.

"All the News That's Fit to Print"

The New York Times.

LATE CITY EDITION

U.S. Weather Bureau Report (Page 59) forecasts: Fair today and tonight. Partly cloudy and mild tomorrow. Temp. range: 52—36; yesterday: 53—41.

VOL. CXIV..No. 39,125. © 1965 by The New York Times Company. Times Square, New York, N.Y. 10036 NEW YORK, MONDAY, MARCH 8, 1965. TEN CENTS

**ALABAMA POLICE USE GAS AND CLUBS TO ROUT NEGROES**

57 Are Injured at Selma as Troopers Break Up Rights Walk in Montgomery

DR. KING IS IN ATLANTA

He Reveals Plans to Lead a New March Tomorrow—Court Action Planned

By ROY REED
Special to The New York Times

SELMA, Ala., March 7—Alabama state troopers and volunteer officers of the Dallas County sheriff's office tore through a column of Negro demonstrators with tear gas, nightsticks and whips here today to enforce Gov. George C. Wallace's order against a protest march from Selma to Montgomery.

At least 17 Negroes were hospitalized with injuries and about 40 more were given emergency treatment for minor injuries and tear gas effects.

The Negroes reportedly fought back with bricks and bottles at one point as they were pushed back into the Negro community, far away from most of a squad of reporters and photographers who had been restrained by the officers.

A witness said that Sheriff James G. Clark and a handful of volunteer possemen were pushed back by flying debris when they tried to herd the angry Negroes into the church where the march had begun.

[In Washington the Justice Department announced that agents of the Federal Bureau of Investigation in Selma had been directed to make a full and prompt investigation and to gather evidence whether

Associated Press Wirephoto

CRUSHING VOTER DEMONSTRATION: Alabama state troopers break up march by protesting Negroes in Selma

**Marines Land to Guard Danang Base; China-Soviet Rift Swaying U.S. Policy**

Force 'Strictly Defensive'—Arrival Is Protested by Hanoi and Peking

By JACK LANGGUTH
Special to The New York Times

SAIGON, South Vietnam, Monday, March 8—United States marines began landing this morning at the bay north of Danang to take up security duties around the large United States jet airfield there.

The marines, in full battle gear, met no opposition from Vietcong guerrillas in the area. South Vietnamese troops and advance marine patrols had secured the coast before the landing.

[North Vietnam and Communist China protested the assignment of the marines as an act of United States aggression, according to The

Washington Is Striving to Influence Moscow Against Militancy

By MAX FRANKEL
Special to The New York Times

WASHINGTON, March 7—The conflict between the Soviet Union and Communist China has become, for the first time, a major element in United States diplomacy.

This development is demonstrated, and sometimes even acknowledged, in many private discussions of the war in Vietnam. It is not mentioned publicly because official comment might influence the delicate triangular relationship developing in Southeast Asia among Moscow, Peking and Washington.

But it is no secret to any

Russians Silent 2 Weeks on British Suggestion for Vietnam Talks

By ANTHONY LEWIS
Special to The New York Times

LONDON, March 7—Britain has made a quiet approach to the Soviet Union in an effort to find some path to negotiations on Vietnam.

Two weeks have passed since this diplomatic feeler was put forward. Not a word has come from Moscow in response.

Sir Humphrey Trevelyan, Britain's Ambassador to Moscow, conveyed the feeler in a message to the Kremlin on Feb. 20. Soviet officials have since been given several reminders that a reply is expected.

The British approach was

**BONN WILL SEEK FORMAL ISRAEL TIE**

West Germany Also Decides to Maintain Diplomatic Relations With Cairo

By ARTHUR J. OLSEN
Special to The New York Times

BONN, March 7—West Germany announced today it was seeking to establish diplomatic relations with Israel.

It will not break relations with the United Arab Republic, at least for the time being.

A Government statement, issued after day-and-night debate in the Government of Chancellor Ludwig Erhard over Middle Eastern policy, said the all-out reception given in Cairo last week to Walter Ulbricht, head of state of Communist East Germany, had been "answered" by Bonn's cutting off further

**GROSS INTEGRATION PLAN BACKS ALLEN ON SCHOOLS; OMITS BUSING AND PAIRING**

**Vast New Program of Aid For Arts Urged on Nation**

A Report by Rockefeller Brothers Fund Cites Need for Support

By RICHARD F. SHEPARD

A vast, comprehensive program of augmented nationwide support for the performing arts is called for in an exhaustive report issued today by the Rockefeller Brothers Fund.

The 55,000-word report, two years in the making, finds that the arts are in trouble despite a cultural boom, and urges increased support by Government at all levels, foundations, business and the public.

The most extensive inventory of its kind ever undertaken here, the report examines the problems, goals and methods of progress for nonprofit, professional performing arts such as resident theater, symphonies, operas and dance troupes.

Its objective is to explore ways to expand the performing arts in the United States

Continued on Page 32, Column 1

Cultural Establishment Is Seeking New Patrons From Broad Base

By MILTON ESTEROW

The city's culture establishment is experiencing a quiet revolution.

Reflecting an era of some of the greatest social changes in the nation's history, with cultural ferment spreading from coast to coast, the city's arts patrons, once a tight little body bounded by social position and great wealth, are being transformed into an expanding group that would have surprised, and perhaps even shocked, grandmother.

"We are swinging away from the patronage of the few to the patronage of the many," a director of Lincoln Center for the Performing Arts says.

The shift is considered far from complete. Increasingly, the city's power structure is being drawn to the arts, resulting in a broadening of corporate giv-

Continued on Page 32, Column 6

REFORMS ADVISED

New Grade Patterns, Shifting of 32,000 Students Urged

Excerpts from Gross report are printed on Page 22.

By LEONARD BUDER

Basic changes in the city school system to provide better integration and improved education were proposed in a report made public yesterday by the Board of Education.

The plan, which would cost $28 million to implement, was prepared under the direction of Dr. Calvin E. Gross, the deposed Superintendent of Schools.

The report did not propose the compulsory assignment of busing of white children to heavily Negro schools to correct racial imbalance. Nor did it recommend any new elementary school pairings or junior high school zoning changes to promote integration.

The introduction of such measures on a limited basis last fall evoked bitter protests from white parents and led to charges that more drastic action would be put into effect next September.

Upholds Allen Report

The report called for the adoption, as the basis for school policy, of the recommendations made last spring by a special advisory committee appointed by Dr. James E. Allen Jr., the

**Moses Asks Garage At 59th St. Bridge; Plan Angers Barnes**

By PETER KIHSS

Robert Moses disclosed a new

**GOVERNOR WARNS ON MINIMUM WAGE**

Tells the Legislature to Link

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[1] Bob Dylan, *The Times They Are a-Changin'* (New York: Columbia Studios. Released as single, March 8, 1965).
[2] *The New York Times*, March 8, 1965.

## Yet, Some Things Never Change

Even though the world may have been brewing with uncertainty and upheaval similar to that which filled the air in 1965, when going through the annual letters to Berkshire Hathaway shareholders, our method of understanding the insurance and float generation strategy of Berkshire will mirror that of Buffett's approach when analyzing potential investments. That is, we won't pre-occupy ourselves with distractions occurring on the macro stage in a given year. We will take a bottoms-up approach by focusing on the fundamentals of Berkshire itself.

Buffett elaborates on this bottoms-up approach in the 1994 shareholder letter and directly references the Vietnam War that had rapidly escalated in 1965, 30 years earlier:

> We will continue to ignore political and economic forecasts, which are an expensive distraction for many investors and businessmen. **Thirty years ago, no one could have foreseen the huge expansion of the Vietnam War**, wage and price controls, two oil shocks, the resignation of a president, the dissolution of the Soviet Union, a one-day drop in the Dow of 508 points, or treasury bill yields fluctuating between 2.8% and 17.4%.
>
> **But, surprise - none of these blockbuster events made the slightest dent in Ben Graham's investment principles. Nor did they render unsound the negotiated purchases of fine businesses at sensible prices.** Imagine the cost to us, then, if we had let a fear of unknowns cause us to defer or alter the deployment of capital. Indeed, we have usually made our best purchases when apprehensions about some macro event were at a peak. Fear is the foe of the faddist, but the friend of the fundamentalist.[3] [emphasis added]

When looking at Berkshire itself, while we will be using Ben Graham's investment principles and Charlie Munger's approach of buying fine businesses at sensible prices, we will be applying this bottoms-up approach on capital flows going in the opposite direction.

In other words, Ben Graham and Charlie Munger are talking about your money going out to pay for future cash flows coming in. We will be exploring other people's money coming in to pay for future cash flows going out (i.e. insurance premiums coming in to fund claims payments going out; other forms of float). Graham and Munger's concepts still apply; margin of safety between the price paid and value received and the power of compounding are just as applicable when analyzing other people's money coming in to pay for future cash flows going out.

Since the first insurance company is not acquired until 1967, we won't be delving into this latter concept until our analysis of the 1967 annual letter. But for now, let's dive into the 1965 shareholder letter.

## The 1965 Shareholder Letter

The 1965 shareholder letter is only one page, so it's very short. But there are some interesting themes that stand out.

### 1. New Representation of Earnings Power

Immediately in the first sentence of the letter, there is something a little odd. The comparable net earnings figure from the prior year, 1964, was changed:

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[3] Warren E. Buffett, 1994 Chairman's Letter (Berkshire Hathaway 1994 Annual Report: 1995).

> The fiscal year ended October 2, 1965, resulted in net earnings of $2,279,206 as compared to net earnings of $125,586 for the prior year.[4]

Net earnings for 1964 were reported as $125,586 in the 1965 shareholder letter. However, if we look at the 1964 shareholder letter, as shown below, the net earnings figure for Berkshire when it was run under previous management was reported higher at $175,586.

**A N N U A L   R E P O R T**

**For the Year Ended October 3, 1964**

November 20, 1964

To the Stockholders of
Berkshire Hathaway Inc.:

The fiscal year ended October 3, 1964 resulted in a profit of $175,586 after depreciation of $1,101,147, and all Divisions of the Company were operating on a profitable basis at the end of the final quarter. [5]

What's going on? Nothing changed in the economic history for Berkshire, nor was this figure a misprint. What happened was a change in accounting or the presentation of financial figures. Another way of putting it would be that Buffett wanted to change the way shareholders of Berkshire held the company accountable. The balance sheet stayed exactly the same, but the presentation of the income statement changed significantly.

Here is the **1965 income statement** showing $125,586 in net earnings for the prior 1964 fiscal year:

| | *1965* | *1964* |
|---|---|---|
| Net sales | $49,300,685 | $49,982,830 |
| Cost of sales | 42,478,984 | 47,382,337 |
| Gross profit | 6,821,701 | 2,600,493 |
| Selling, general and administrative expenses | 2,135,038 | 2,072,822 |
| Operating income | 4,686,663 | 527,671 |
| Other deductions, net | 127,348 | 126,060 |
| Idle plant expense | 240,109 | 226,025 |
| | 367,457 | 352,085 |
| Earnings before charge equivalent to Federal income taxes | 4,319,206 | 175,586 |
| Charge equivalent to Federal income taxes (*Note C*) | 2,040,000 | 50,000 |
| Net earnings | $ 2,279,206 | $ 125,586 |
| Depreciation and amortization | $ 862,424 | $ 1,101,147 [6] |

When we look at the **1964 income statement**, however, net earnings for 1964 is shown as $175,586:

[4] Warren E. Buffett, *Berkshire Hathaway Letters to Shareholders 1965-2013* (Berkshire Hathaway Annual Reports: 2014), p. 1.
[5] Warren E. Buffett, *2014 Chairman's Letter* (Berkshire Hathaway 2014 Annual Report: 2015), p. 133.
[6] Berkshire Hathaway Inc. (1965). *Form 10-K 1965*.

| | Years Ended | |
|---|---|---|
| | October 3, 1964 | September 28, 1963 |
| SALES | $49,982,830 | $50,590,679 |
| Cost of sales, administrative and selling expenses | 48,354,012 | 49,418,947 |
| Depreciation | 1,101,147 | 1,716,613 |
| | 49,455,159 | 51,135,560 |
| OPERATING PROFIT (LOSS) | 527,671 | (544,881) |
| Other income | 111,849 | 307,140 |
| | 639,520 | (237,741) |
| Other deductions | 237,909 | 309,733 |
| NET EARNINGS (LOSS) BEFORE IDLE PLANT EXPENSE | 401,611 | (547,474) |
| Idle plant expense | 226,025 | 137,337 |
| NET EARNINGS (LOSS) | $ 175,586 | $ (684,811) |

[7]

Why did Buffett want to show lower earnings? He did so to bring down shareholder expectations for future performance to more realistic levels, by portraying a more accurate representation of recurring earnings power.

He explained in the 1965 shareholder letter that actual net earnings in 1965 and 1964 were artificially boosted by tax-deductible operating losses carried over from previous years and that any assessment on future performance should be based on normalized earnings that take into account regularly occurring taxes. Hence, a new line item, "Charge equivalent to Federal income taxes", appeared in the 1965 income statement right above net earnings. In the 1965 shareholder letter, Buffett explained the rationale for the addition of this new line item, as follows:

> Because of loss carryovers, no federal income taxes were payable by the Corporation with respect to either of these years; however to prevent any misleading interpretation of future earnings when loss carryovers shall not be available, the Corporation had included in computing net earnings for 1965 and 1964 a charge substantially equal to the federal income taxes that would be payable with respect to results of operations during each of these years.[8]

Some other significant changes in the presentation of the income statement were the major line items flowing from net sales down to operating income. While 1964 sales and operating income were reported the same, $49,982,830 and $527,671, respectively, in both the 1965 and 1964 income statements shown above, the line items in between were very different.

The 1964 income statement starts with "Sales" and deducts "Cost of sales, administrative and selling expenses" and "Depreciation" to arrive at "Operating Profit (Loss)".

The problem for an investor looking at such figures is that it's difficult to discern what costs are directly related to the production of the goods produced by Berkshire. The cost of sales or cost of good sold (COGS) consists of costs of the materials used to manufacture product (inventory) along with the direct labor costs used to produce this inventory. Such cost of sales would exclude indirect

[7] Warren E. Buffett, *2014 Chairman's Letter* (Berkshire Hathaway 2014 Annual Report: 2015), p. 138.
[8] Warren E. Buffett, *Berkshire Hathaway Letters to Shareholders 1965-2013* (Berkshire Hathaway Annual Reports: 2014), p. 1.

expenses such as distribution costs and sales force and advertising costs. The 1964 income statement, however, lumps all these direct and indirect expenses together, making the calculation of gross profit difficult.

Under Buffett, the 1965 income statement, as shown above, fixed this problem by presenting costs more transparently. It starts with "Net Sales" and deducts "Cost of sales", resulting in "Gross profit", from which "Selling, general and administrative expenses" is then deducted to arrive at "Operating Income". This is a much more transparent way of presenting the operating performance of Berkshire, as investors can assess how well management is managing costs directly related to the manufacturing of its goods and whether revenues from the sales of such goods are resulting in a sufficient gross profit. Furthermore, it also enables investors to more easily assess how well the company is managing its selling, general and administrative (SG&A) expenses, which are not directly related to the manufacturing of the core products.

**2. Earnings Finally Positive, But Not All Roses**

In addition to adjusting net earnings downward with normalized taxes, Buffett poured even more realism on the parade for investors. In the 1965 letter, he implied that even though net earnings in 1964 and 1965 were finally positive for the first time since 1960, thus increasing total shareholders' equity or book value, such positive contributions to book value don't take into account losses suffered from the disposal of assets related to the closing of two major plants. He wrote in the 1965 shareholder letter:

> The fiscal year ended October 2, 1965, resulted in net earnings of $2,279,206 as compared to net earnings of $125,586. These net earnings do not reflect any nonrecurring losses incurred on the disposal of assets due to the permanent closing of the King Philip Plants A and E in Fall River, Massachusetts, as such losses have been charged to a reserve previously established for such purpose.[9]

In fact, the positive net earnings contributed to retained earnings in 1964 and 1965 were more than offset by estimated losses on future asset disposals during the same time period. Looking below at the 1965 statement of retained earnings, a major driver of overall change in book value or change shareholders' equity, one will notice $300,000 charged against surplus in 1965 and $3,000,000 charged against surplus in 1964. So, even though net earnings normalized for taxes from the past two years were $2,404,792 ($2,279,206 in 1965 + $125,586 in 1964), this positive contribution is more than offset by a contemporaneous charge of $3,300,000 of estimated losses on properties to be sold.

**CONSOLIDATED STATEMENT OF RETAINED EARNINGS**

| | | |
|---|---|---|
| BALANCE AT BEGINNING OF YEAR | $19,417,576 | $22,241,990 |
| Net earnings for the year | 2,279,206 | 125,586 |
| Credit resulting from charge equivalent to Federal income taxes (*Note C*) | 2,040,000 | 50,000 |
| Retirement of treasury stock (*Note E*) | (2,967,714) | —0— |
| Estimated loss on properties to be sold | (300,000) | (3,000,000) |
| BALANCE AT END OF YEAR | $20,469,068 | $19,417,576 |

[10]

[9] Ibid.
[10] Berkshire Hathaway Inc. (1965). *Form 10-K 1965*.

The $3,000,000 charge incurred in 1964 was specifically designated to cover estimated losses stemming from the disposal of King Philip E Division, the liquidation of which began in 1964.[11] However, this poses an interesting timing issue because, as per the 1965 shareholder letter, a major chunk of this asset disposal occurred in the following 1965 fiscal year. So to which fiscal year should the $3,000,000 charge belong? Such are the frequent shortcomings of accounting and managerial reporting of financials, be it during 1965 or today. Buffett elaborates on this King Philip E Division liquidation in the 1965 shareholder letter, as follows:

> A major portion of the machinery at King Philip Plant E Division has been sold. We expect to dispose of the remaining portion of this plant during the current [1966] fiscal year. This will complete the liquidation of our unprofitable plants. The proposed sale of the King Philip E Division will make it necessary to provide storage for raw cotton and grey cloth for the King Philip D Division at the Hathaway Division Plant C (former Langshaw Mill). Plans are underway to accomplish this within the current [1966] fiscal year.[12]

While it's a comfort that these estimated losses on properties to be sold are deemed non-recurring, the fact that such significant charges are not shown on the income statement is a reminder that simply looking at the earnings report or income statement can be an incomplete or misleading representation of a company's performance. This was one of the reasons why Ben Graham was focused so heavily on the balance sheet, as a balance sheet's snapshot in time was less prone to similar, habitual beautification by management of a reporting period's operating figures (i.e. income statement). On the flip side, simply looking at the income statement would not have allowed investors to recognize $2,967,714 was spent in 1965 in share repurchases, resulting in a decline in the number of shares outstanding, a positive for shareholders all else being equal.

### 3. Liquidity, Liquidity, Liquidity

Two ways to generate more cash on the balance sheet are to better manage balance sheet items such as working capital and to increase cash flows via higher operating margins. Both of these were achieved in 1965. Buffett goes into the balance sheet and the income statement improvements achieved during the year in the 1965 shareholder letter:

> During 1965 raw material, stock in process and cloth inventories were decreased by $1,411,967 and bank loans of $2,500,000 were paid off. Also, during the year, the Corporation purchased 120,231 of its own shares, leaving a total of 1,017,547 shares outstanding at the end of the fiscal year.
>
> The Corporation made a substantial reduction in its overhead costs during the fiscal year just ended. Approximately $811,812 was invested by the Corporation during the year in the purchase of new machinery in a continuing effort to reduce costs and to improve quality. This program will continue during the current [1966] fiscal year.[13]

The following table shows the increase in working capital from 1964 to 1965:

| Supplemental data | 10/3/1964 | 10/2/1965 |
|---|---|---|
| Working capital | 14,502,068 | 17,869,526 |
| *y-o-y growth %* | *-16.7%* | *23.2%* |
| Working capital per share | $12.75 | $17.56 |
| *y-o-y growth %* | *17.7%* | *37.8%* |

[11] Warren E. Buffett, *2014 Chairman's Letter* (Berkshire Hathaway 2014 Annual Report: 2015), p. 135.
[12] Warren E. Buffett, *Berkshire Hathaway Letters to Shareholders 1965-2013* (Berkshire Hathaway Annual Reports: 2014), p. 1.
[13] Ibid.

While working capital increased, liquidity also improved significantly as less cash was tied up in inventory, the bank note was paid off and cash and marketable securities increased from $920,089 in 1964 to $3,675,504 in 1965 ($775,504 cash + $2,900,000 marketable securities & certificates of deposit), as shown in the table below.

Furthermore, per the analysis shown in the table below, management of working capital improved as:

- Inventory was turned over faster in 1965 with average days inventory outstanding decreasing from 117 days to 94 days
- Average days sales outstanding improved slightly, declining one day to 55 days, while average days payable outstanding also improved slightly, increasing two days to 20 days
- In summary, the cash conversion cycle or the average time it took Berkshire to pay for its inventory, sell this inventory and finally receive cash from the sale decreased significantly from 117 days to 94 days

| **Working capital** | **10/3/1964** | **10/2/1965** |
|---|---|---|
| *($USD, except share count figures)* | | |
| Cash | 920,089 | 775,504 |
| Marketable securities & certificates of deposit | 0 | 2,900,000 |
| Accounts receivable | 7,450,564 | 7,422,726 |
| Inventories | 11,689,145 | 10,277,178 |
| Prepaid insurance, taxes and other expense | 190,563 | 196,391 |
| **Current assets** | **20,250,361** | **21,571,799** |
| Notes payable - banks | 2,500,000 | 0 |
| Accounts payable | 2,096,726 | 2,581,585 |
| Accrued wages & salaries | 294,764 | 296,256 |
| Accrued state & local taxes | 365,112 | 441,951 |
| Social security & withholding taxes payable | 491,691 | 382,481 |
| **Current liabilities** | **5,748,293** | **3,702,273** |
| **Working capital** | **14,502,068** | **17,869,526** |

| **Working capital management:** | **10/3/1964** | **10/2/1965** |
|---|---|---|
| Days in fiscal year | 372 | 365 |
| Inventory BOP | 18,011,345 | 11,689,145 |
| Inventory EOP | 11,689,145 | 10,277,178 |
| Avg. inventory | 14,850,245 | 10,983,162 |
| **Inventory turnover (COGS/Avg. inventory)** | **3.2x** | **3.9x** |
| **Days inv. outstanding (Avg. inv./COGS*Days in period)** | **117** | **94** |
| Accounts receivable BOP | 7,670,236 | 7,450,564 |
| Accounts receivable EOP | 7,450,564 | 7,422,726 |
| Avg. AR | 7,560,400 | 7,436,645 |
| **Days sales outstanding (Avg. AR/Sales*Days in period)** | **56** | **55** |
| Accounts payable BOP | 2,415,395 | 2,096,726 |
| Accounts payable EOP | 2,096,726 | 2,581,585 |
| Avg. AP | 2,256,061 | 2,339,156 |
| **Days payable outstanding (Avg. AP/COGS*Days in** | **18** | **20** |

| | | |
|---|---|---|
| **period)** | | |
| **Cash conversion cycle (DIO+DSO-DPO)** | **155** | **129** |

As per the 1965 shareholder letter, only four divisions located at two sites are continuing to be operated by Berkshire as of the end of 1965 fiscal year-end:

1. King Phillip Plant D in Warren, Rhode Island;
2. Hathaway Synthetic, Box Loom and Home Fabrics Divisions in New Bedford, Massachusetts.[14]

While most of the buildings and machinery at King Phillip Plant A Division were sold during the 1964 fiscal year, a major portion of the King Phillip Plant E Division asset disposals were accomplished in the 1965 fiscal year. When an unprofitable plant gets shut down, any inventory stored at the closed plants can still be sold off.

While the inventory may have to be stored elsewhere, the expenses incurred (i.e. overhead, labor, etc.) from the operation of the unprofitable plants can come to a halt. This likely explains part of the yearly decline of 11.6% in payroll from $13,135,731 to $11,618,517, as per the table below.

| Supplemental data | 10/3/1964 | 10/2/1965 |
|---|---|---|
| Payroll | 13,135,731 | 11,618,517 |
| *y-o-y growth %* | *-18.4%* | *-11.6%* |

The analysis below clearly indicates a massive improvement year-over-year in operating margins from 1964 to 1965, as gross profit margin increased from 5.2% to 13.8%, operating income margin increased from 1.1% to 9.5% and net earnings margin increased from a paltry 0.3% to 4.6%:

| Operating statistics | 10/3/1964 | 10/2/1965 |
|---|---|---|
| **Y-O-Y growth:** | | |
| Sales | -1.2% | -1.4% |
| Gross profit | NA | 162.3% |
| Operating income | -196.8% | 788.2% |
| Earnings before charge equiv. to Federal inc. taxes | NA | 2359.9% |
| Net earnings | NA | 1714.9% |
| EPS | NA | 1929.3% |
| | **10/3/1964** | **10/2/1965** |
| **Margins:** | | |
| **Sales** | **100.0%** | **100.0%** |
| Cost of sales | 94.8% | 86.2% |
| **Gross profit** | **5.2%** | **13.8%** |
| Selling, general & administrative expenses | 4.1% | 4.3% |
| **Operating income** | **1.1%** | **9.5%** |
| Other deductions, net | 0.3% | 0.3% |
| Idle plant, expense | 0.5% | 0.5% |
| Other operating expenses | 0.7% | 0.7% |

[14] Ibid.

| | | |
|---|---|---|
| **Earnings before charge equiv. to Federal inc. taxes** | **0.4%** | **8.8%** |
| Charge equivalent to Federal inc. taxes | 0.1% | 4.1% |
| **Net earnings** | **0.3%** | **4.6%** |
| Depreciation & amortization | 2.2% | 1.7% |
| **Implied tax rate** | **28.5%** | **47.2%** |

## 4. Outlook

Seabury Stanton resigned as a director and President, with Kenneth V. Chace elected by the board as successor. John K. Stanton resigned as director and as Treasurer and Clerk with Harold V. Banks elected as the new Treasurer and Clerk.

This was perhaps the coldest send-off one might expect in a public statement regarding the termination of a long-standing director and President, whose family had owned and operated the business for decades. While acknowledging "fifty years of service" given by Seabury Stanton, there is nothing close to a "thank you" or other semblance of gratitude. This send-off is in stark comparison to the expression only a few lines later of "thanks to all the employees of the Corporation whose loyal cooperation and efforts have helped to make this year successful."[15] The 1965 fiscal year ended with significant backlogs of unfilled order at all divisions, and management expects the coming 1966 fiscal year to continue to be profitable.

Interestingly, the 1965 letter ends with the names of Chairman of the Board Malcolm G. Chace, Jr., and President Kenneth V. Chace appearing at the bottom. However, the compilation of letters compiled in *Berkshire Hathaway Letters to Shareholders, 2013*, denotes the 1965 letter as a "[Letter written by Warren E. Buffett]".[16]

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[15] Warren E. Buffett, *Berkshire Hathaway Letters to Shareholders 1965-2013* (Berkshire Hathaway Annual Reports: 2014), p. 1.
[16] Ibid.

## 5. Financials

| Berkshire Hathaway | | |
|---|---|---|
| **Fiscal Year** | **1964** | **1965** |
| *($USD, except share count figures)* | | |
| **Balance Sheet** | **10/3/1964** | **10/2/1965** |
| **Assets** | | |
| Current assets: | | |
| Cash | 920,089 | 775,504 |
| Marketable securities & certificates of deposit | 0 | 2,900,000 |
| Accounts receivable | 7,450,564 | 7,422,726 |
| Inventories | 11,689,145 | 10,277,178 |
| Prepaid insurance, taxes and other expense | 190,563 | 196,391 |
| **Total current assets** | **20,250,361** | **21,571,799** |
| Properties, plant & equipment: | | |
| Properties comprising land, buildings, machinery & equip. | 33,635,553 | 28,019,742 |
| Less accumulated depreciation and amortization | 21,853,689 | 19,593,163 |
| **Net PP&E** | **11,781,864** | **8,426,579** |
| Less estimated loss on properties to be sold | 4,210,621 | 1,809,132 |
| **Total carrying value of Net PP&E** | **7,571,243** | **6,617,447** |
| Mortgage notes receivable & other assets | 65,442 | 33,141 |
| **Total assets** | **27,887,046** | **28,222,387** |
| **Liabilities & stockholders' equity** | | |
| **Liabilities** | | |
| Current liabilities: | | |
| Notes payable - banks | 2,500,000 | 0 |
| Accounts payable | 2,096,726 | 2,581,585 |
| Accrued wages & salaries | 294,764 | 296,256 |
| Accrued state & local taxes | 365,112 | 441,951 |
| Social security & withholding taxes payable | 491,691 | 382,481 |
| **Total current liabilities** | **5,748,293** | **3,702,273** |
| **Stockholders' equity** | | |
| Common stock | 8,036,900 | 5,688,890 |
| Retained earnings | 19,417,576 | 20,469,068 |
| Common stock & retained earnings | 27,454,476 | 26,157,958 |
| Less common stock in treasury at cost | 5,315,723 | 1,637,844 |
| **Total stockholders' equity** | **22,138,753** | **24,520,114** |
| **Total liabilities & stockholders' equity** | **27,887,046** | **28,222,387** |

| Income statement | 10/3/1964 | 10/2/1965 |
|---|---|---|
| **Sales** | **49,982,830** | **49,300,685** |
| Cost of sales | 47,382,337 | 42,478,984 |
| **Gross profit** | **2,600,493** | **6,821,701** |
| Selling, general & administrative expenses | 2,072,822 | 2,135,038 |
| **Operating income** | **527,671** | **4,686,663** |
| Other deductions, net | 126,060 | 127,348 |
| Idle plant, expense | 226,025 | 240,109 |
| Other operating expenses | 352,085 | 367,457 |
| **Earnings before charge equiv. to Federal inc. taxes** | **175,586** | **4,319,206** |
| Charge equivalent to Federal inc. taxes | 50,000 | 2,040,000 |
| **Net earnings** | **125,586** | **2,279,206** |
| Depreciation & amortization | 1,101,147 | 862,424 |

| Change in retained earnings | 10/3/1964 | 10/2/1965 |
|---|---|---|
| **Balance at beginning of year** | **22,241,990** | **19,417,576** |
| Net earnings (loss) for the year | 125,586 | 2,279,206 |
| Credit resulting from charge equiv. to Federal inc. taxes | 50,000 | 2,040,000 |
| Retirement of treasury stock | 0 | (2,967,714) |
| Estimated loss on properties to be sold | (3,000,000) | (300,000) |
| **Balance at end of year** | **19,417,576** | **20,469,068** |

| Supplemental data | 10/3/1964 | 10/2/1965 |
|---|---|---|
| Shares outstanding | 1,137,778 | 1,017,547 |
| *y-o-y growth %* | *-29.2%* | *-10.6%* |
| Earnings per share | $0.11 | $2.24 |
| *y-o-y growth %* | *NMF* | *1929.3%* |
| Working capital | 14,502,068 | 17,869,526 |
| *y-o-y growth %* | *-16.7%* | *23.2%* |
| Working capital per share | $12.75 | $17.56 |
| *y-o-y growth %* | *17.7%* | *37.8%* |
| Total stockholders' equity | 22,138,753 | 24,520,114 |
| *y-o-y growth %* | *-26.9%* | *10.8%* |
| Total stockholders' equity per share | $19.46 | $24.10 |
| *y-o-y growth %* | *3.3%* | *23.8%* |
| Payroll | 13,135,731 | 11,618,517 |
| *y-o-y growth %* | *-18.4%* | *-11.6%* |
| Additions to properties & equipment | 288,608 | 811,812 |
| *y-o-y growth %* | *-56.7%* | *181.3%* |
| Depreciation & amortization | 1,101,147 | 862,424 |
| *y-o-y growth %* | *-35.9%* | *-21.7%* |

# BERKSHI

## CONSOLIDAT

with

—— ASSETS ——

| | 1965 | 1964 |
|---|---|---|
| CURRENT ASSETS: | | |
| Cash | $ 775,504 | $ 920,089 |
| Marketable securities (including $2,600,000 of short term certificates of deposit), at cost, approximate market | 2,900,000 | —0— |
| Accounts receivable (less allowance for doubtful accounts — 1965 — $280,302) | 7,422,726 | 7,450,564 |
| Inventories (*Note A*) | 10,277,178 | 11,689,145 |
| Prepaid insurance, taxes and other expense | 196,391 | 190,563 |
| TOTAL CURRENT ASSETS | 21,571,799 | 20,250,361 |
| PROPERTIES, PLANTS AND EQUIPMENT (*Note B*): | | |
| Properties comprising land, buildings, machinery and equipment | 28,019,742 | 33,635,553 |
| Less accumulated depreciation and amortization | 19,593,163 | 21,853,689 |
| | 8,426,579 | 11,781,864 |
| Less estimated loss on properties to be sold | 1,809,132 | 4,210,621 |
| | 6,617,447 | 7,571,243 |
| MORTGAGE NOTES RECEIVABLE AND OTHER ASSETS | 33,141 | 65,442 |
| TOTAL ASSETS | $28,222,387 | $27,887,046 |

# HATHAWAY INC.

## BALANCE SHEET

**1965**
**res for 1964**

### —LIABILITIES AND STOCKHOLDERS' EQUITY—

| | *1965* | *1964* |
|---|---|---|
| CURRENT LIABILITIES: | | |
| Notes payable — banks | $ —0— | $ 2,500,000 |
| Accounts payable | 2,581,585 | 2,096,726 |
| Accrued wages and salaries | 296,256 | 294,764 |
| Accrued state and local taxes | 441,951 | 365,112 |
| Social security and withholding taxes payable | 382,481 | 491,691 |
| TOTAL CURRENT LIABILITIES | 3,702,273 | 5,748,293 |
| STOCKHOLDERS' EQUITY: | | |
| Common stock ($5 par value) authorized 1,843,214 shares — issued 1,137,778 shares (*Note E*) | 5,688,890 | 8,036,900 |
| Retained earnings | 20,469,068 | 19,417,576 |
| | 26,157,958 | 27,454,476 |
| Less common stock in treasury at cost — 120,231 shares (*Note E*) | 1,637,844 | 5,315,723 |
| | 24,520,114 | 22,138,753 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $28,222,387 | $27,887,046 |

# Berkshire Hathaway Inc.

## CONSOLIDATED STATEMENT OF EARNINGS

### YEAR ENDED OCTOBER 2, 1965
with comparative figures for 1964

| | *1965* | *1964* |
|---|---|---|
| Net sales | $49,300,685 | $49,982,830 |
| Cost of sales | 42,478,984 | 47,382,337 |
| Gross profit | 6,821,701 | 2,600,493 |
| Selling, general and administrative expenses | 2,135,038 | 2,072,822 |
| Operating income | 4,686,663 | 527,671 |
| Other deductions, net | 127,348 | 126,060 |
| Idle plant expense | 240,109 | 226,025 |
| | 367,457 | 352,085 |
| Earnings before charge equivalent to Federal income taxes | 4,319,206 | 175,586 |
| Charge equivalent to Federal income taxes (*Note C*) | 2,040,000 | 50,000 |
| Net earnings | $ 2,279,206 | $ 125,586 |
| Depreciation and amortization | $ 862,424 | $ 1,101,147 |

## CONSOLIDATED STATEMENT OF RETAINED EARNINGS

| | | |
|---|---|---|
| Balance at beginning of year | $19,417,576 | $22,241,990 |
| Net earnings for the year | 2,279,206 | 125,586 |
| Credit resulting from charge equivalent to Federal income taxes (*Note C*) | 2,040,000 | 50,000 |
| Retirement of treasury stock (*Note E*) | (2,967,714) | —0— |
| Estimated loss on properties to be sold | (300,000) | (3,000,000) |
| Balance at end of year | $20,469,068 | $19,417,576 |

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SECURITIES AND EXCHANGE COMMISSION
Washington, D. C.
20549

FORM 10-K

RECEIVED
U. S. SECURITIES & EXCHANGE COMMISSION
FEB 1 - 1966

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

For the fiscal year ended October 2, 1965

Commission file number 0-853

BERKSHIRE HATHAWAY INC
(Exact name of registrant as specified in its charter)

MASSACHUSETTS
(State or other jurisdiction of incorporation or organization)

04-225-4452
(I.R.S. Employer Identification No.)

97 COVE STREET, NEW BEDFORD, MASSACHUSETTS
(Address of principal executive offices)

02741
(Zip Code)

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

NONE

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

COMMON STOCK, $5 PAR VALUE
(Title of Class)

BERKSHIRE HATHAWAY INC.

FORM 10-K

JANUARY 28, 1966

Item 1. Number of Equity Security Holders

| (A) Title of class | (B) Approximate number of record holders January 21, 1966 |
|---|---|
| Common stock, $5 par value | 2,950 |

Item 2. Increases and Decreases in Outstanding Equity Securities

No increase or decrease in outstanding equity securities has occurred except for the changes previously reported in Form 8-K, Current Report for the Month of December 1965, filed with the Securities and Exchange Commission pursuant to transmittal letter dated December 31, 1965, which 8-K hereby is incorporated by reference.

Item 3. Parents and Subsidiaries of Registrant

As of January 21, 1966 Buffett Partnership, Ltd., a limited partnership under Nebraska law, owned approximately 54.3% of Registrant's outstanding shares. Mr. Warren E. Buffett, a director of the Registrant, is the sole general partner of the partnership.

Items 4 to 9, inclusive

These items are not restated or inserted by the Registrant inasmuch as since the close of its fiscal year ended October 2, 1965 the Registrant has filed with the Commission a definitive Proxy Statement pursuant to Regulation 14A which involved, among other things, the election of Directors and which Proxy Statement was transmitted to the Securities and Exchange Commission by letter dated November 10, 1965.

Item 10. Financial Statements and Exhibits

(a) See financial statements and auditor's certificate attached.

(b) Exhibits - NONE

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Annual Report to be signed on its behalf by the undersigned thereunto duly authorized.

BERKSHIRE HATHAWAY INC.

By Kenneth V. Chace
Kenneth V. Chace
President

DATED: January 28, 1966

RECEIVED
U. S. SECURITIES & EXCHANGE COMMISSION
FEB 1 - 1966

Item 10(a) Financial Statements

Consolidated financial statements for the year ended October 2, 1965:

Accountants' Report

Consolidated Balance Sheet as of October 2, 1965

Consolidated Statement of Earnings and Retained Earnings for the year ended October 2, 1965

Notes to Consolidated Financial Statements

Schedule V Property, plant and equipment

Schedule VI Accumulated depreciation of property, plant and equipment

Schedule XII Reserves

All other schedules are omitted as the required information is inapplicable or the information is presented in the financial statements or related notes.

The financial statements of the registrant are omitted as it is primarily an operating company and its subsidiary included in the consolidated financial statements is totally held.

ACCOUNTANTS' REPORT

The Board of Directors
Berkshire Hathaway Inc.:

We have examined the consolidated financial statements and related schedules of Berkshire Hathaway Inc. and 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.

In our opinion, such financial statements present fairly the consolidated financial position of Berkshire Hathaway Inc. and subsidiary at October 2, 1965, and the results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year except for the treatment of the Charge equivalent to Federal income tax as explained in Note 4 of notes to consolidated financial statements. The supporting schedules, in our opinion, present fairly the information required to be stated therein.

Peat Marwick Mitchell & Co

Providence, R. I.
October 28, 1965

BERKSHIRE HATHAWAY INC.

Consolidated Balance Sheet

October 2, 1965

## Assets

| | | |
|---|---|---|
| Current assets: | | |
| Cash | | $ 775,504 |
| Marketable securities (including $2,600,000 of short-term certificates of deposit), at cost, approximate market | | 2,900,000 |
| Accounts receivable - trade, including $4,562 due from officers and employees, net of allowance for doubtful accounts ($280,302) (Schedule XII) | | 7,422,726 |
| Inventories (note 2) | | 10,277,178 |
| Prepaid expenses | | 196,391 |
| Total current assets | | 21,571,799 |
| Property, plant and equipment, at cost (note 3) (Schedule V): | | |
| Land | $ 142,514 | |
| Buildings | 4,432,512 | |
| Machinery and equipment | 23,025,457 | |
| Furniture and fixtures | 355,931 | |
| Leasehold improvements | 23,429 | |
| Motor vehicles | 39,899 | |
| | 28,019,742 | |
| Less accumulated depreciation and amortization (Schedule VI) | 19,593,163 | |
| | 8,426,579 | |
| Less allowance for estimated loss on properties to be sold (Schedule XII) | 1,809,132 | 6,617,447 |
| Other assets (including mortgage note of approximately $21,700 due from officer) | | 33,141 |
| | | $ 28,222,387 |

## Liabilities and Stockholders' Equity

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | | $ 2,964,066 |
| Accrued salaries and wages | | 296,256 |
| Accrued state and local taxes | | 441,951 |
| Total current liabilities | | 3,702,273 |
| Stockholders' equity (notes 1 and 5): | | |
| Common stock $5 par value. 1,843,214 shares authorized; 1,137,778 shares issued | $ 5,688,890 | |
| Retained earnings | 20,469,068 | |
| | 26,157,958 | |
| Less 120,231 shares of treasury stock, at cost | 1,637,844 | 24,520,114 |
| Commitments and contingencies (notes 6 and 7) | | |
| | | $ 28,222,387 |

See accompanying notes to financial statements.

BERKSHIRE HATHAWAY INC.

Consolidated Statement of Earnings and Retained Earnings

Year ended October 2, 1965

| | |
|---|---|
| Net sales | $ 49,300,685 |
| Cost of sales (note 2) | 42,478,984 |
| Gross profit | 6,821,701 |
| Selling, general and administrative expenses | 2,135,038 |
| Operating income | 4,686,663 |
| Other income: | |
| Interest on marketable securities | 41,737 |
| Sundry other income | 161,386 |
| | 203,123 |
| | 4,889,786 |
| Other deductions: | |
| Idle plant expense | 240,109 |
| Interest | 33,763 |
| Bad debts | 120,000 |
| State income taxes | 170,000 |
| Sundry other charges | 6,708 |
| | 570,580 |
| Earnings before charge equivalent to Federal income tax | 4,319,206 |
| Charge equivalent to Federal income tax (note 4) | 2,040,000 |
| Net earnings | 2,279,206 |
| Special charge: | |
| Estimated loss on properties to be sold (note 3) | 300,000 |
| Net earnings less special charge | 1,979,206 |
| Retained earnings at beginning of year | 19,417,576 |
| Credit resulting from charge equivalent to Federal income tax (note 4) | 2,040,000 |
| | 23,436,782 |
| Deduct: | |
| Excess of cost of treasury stock retired over par value | 2,967,714 |
| Retained earnings at end of year | $ 20,469,068 |
| Depreciation deducted in above statement | $ 862,424 |

See accompanying notes to financial statements.

BERKSHIRE HATHAWAY INC.

Notes to Consolidated Financial Statements

October 2, 1965

(1) The consolidated financial statements include the accounts of Berkshire Hathaway Inc. and its wholly-owned Canadian subsidiary.

Canadian currency has been converted into United States dollars as follows: (1) current assets and liabilities at rates of exchange in effect at the close of the year, (2) properties at rates in effect when acquired, and (3) income, costs and expenses at average rates of exchange for the year, except depreciation, and amortization which are based on the dollar costs of the properties. The net unrealized loss on such conversions (not significant) has been carried to income.

The excess of the Company's cost over its equity in its subsidiary ($190,330) representing losses since acquisition has been charged to retained earnings in consolidation.

Intercompany balances and transactions have been eliminated in preparing the consolidated financial statements.

Berkshire Hathaway Inc. had no other investments in foreign or domestic affiliates.

(2) The inventories used in the computation of cost of sales were as follows:

October 3, 1964 - $11,689,145
October 2, 1965 - $10,277,178

At October 2, 1965, inventories consisted of the following:

| | |
|---|---|
| Raw materials | $ 2,605,084 |
| Work in process | 2,910,974 |
| Finished goods | 4,585,627 |
| Supplies | 175,493 |
| | $ 10,277,178 |

Raw materials and materials in process are priced at the lower of cost or market, except for the cotton content of stock in process of King Philip D Division which is priced at a standard established in 1933, which is less than the current market. At October 2, 1965 the replacement cost of the cotton, so valued, was approximately $117,000 in excess of the amount at which it is stated in the inventory. Current standard costs are used in valuing labor and manufacturing burden in stock in process. Cloth is priced at the lower of cost or market. All costs were determined generally on an average basis.

The inventory of the subsidiary is priced at the lower of cost or market on a first-in, first-out basis.

(Continued)

BERKSHIRE HATHAWAY INC.

Notes to Consolidated Financial Statements, Continued

(3) At October 2, 1965, there were reserves of $1,809,132 for estimated losses on properties to be sold. These reserves were established to adjust the book values of discontinued operations to estimated realizable values. In the accompanying financial statements an addition to these reserves of $300,000 has been reflected as a special charge against earnings. This amount has been reported to stockholders as a charge against retained earnings.

Upon the sale or retirement of plant and equipment, the applicable accumulated depreciation is eliminated from the accumulated allowance, and the profit or loss resulting from such sale or retirement is reflected in either earnings or estimated loss on properties to be sold.

Depreciation on acquisitions prior to fiscal year ended October 2, 1965 has been charged to operations on the straight-line method. For additions in the current year, depreciation has been computed on the double declining balance method. This change did not have a material effect on earnings. Leasehold improvements are being amortized over the lives of the leases.

Maintenance, repairs, and renewals of a minor nature are charged to income as incurred. Renewals of a major nature and betterments which extend the useful life of plant and equipment are capitalized.

No items of plant and equipment were pledged to secure any indebtedness.

(4) No Federal tax is payable with respect to the net earnings for the year ended October 2, 1965 due to operating loss carryovers and losses on plant assets. These latter losses were charged against the reserve for estimated losses on properties to be sold. However, to prevent a misleading interpretation of future earnings after these losses have been fully utilized, a charge equivalent to the Federal income tax which would have been payable for the year ended October 2, 1965 had these losses not been available, has been reflected as a charge to earnings, and the amount of tax savings due to these losses has been reflected as a credit to retained earnings. If the Company had followed this practice in the prior year, it would have resulted in a charge of approximately $50,000 against earnings in that year.

The Company has unused Federal income tax loss carryovers of approximately $3,450,000 of which approximately $1,200,000 expires in 1967 and the remainder in succeeding years.

Federal income tax returns of the Company have been examined through the fiscal year ended September 30, 1957. The statute of limitations has expired for the fiscal years 1958 through 1961.

(Continued)

BERKSHIRE HATHAWAY INC.

Notes to Consolidated Financial Statements, Continued

(5) At the annual meeting of stockholders held December 1, 1964, it was voted that the authorized capital stock of this Corporation be reduced to 1,843,214 shares of $5 par value common stock by canceling and retiring the 469,602 shares held in the treasury at October 3, 1964 and that the excess of cost over par value of retired shares be charged to retained earnings.

Subsequent to December 1, 1964, the Company purchased an additional 120,231 shares of common stock for the treasury. These shares are carried on the accompanying consolidated balance sheet at cost, $1,637,844.

(6) The Company has in effect a pension plan to provide eligible employees with pension and death benefits. Eligible employees consist of salaried personnel. The unfunded past service cost and annual contribution to the plan by the Company for the year ended October 2, 1965 are $722,700 and $20,871, respectively.

(7) The Company occupies office and warehouse space under long-term leases which call for total annual payments of $66,000 and aggregate rentals of $238,000 over the lives of such leases.

The Company is contingently liable for approximately $147,000 at October 2, 1965 under a union contract covering certain employees who have reached the specified retirement age, have a minimum of fifteen years service, and who retire voluntarily.

The Company has no stock option plans or profit-sharing plans in effect at October 2, 1965.

(8) Supplementary profit and loss information:

| | Charged directly to profit and loss | | |
|---|---|---|---|
| | To cost of sales | Other | Total |
| Maintenance and repairs | $ 356,440 | 27,369 | 383,809 |
| Depreciation and amortization | 816,361 | 46,063 | 862,424 |
| Taxes, other than income taxes: | | | |
| Payroll taxes | 714,747 | 34,638 | 749,385 |
| Real estate and personal property taxes | 108,853 | 63,598 | 172,451 |
| Other state and local taxes | 76,580 | 31,123 | 107,703 |
| | $ 900,180 | 129,359 | 1,029,539 |
| Rents | $ 17,059 | 130,058 | 147,117 |

There were no royalty agreements, no management or service contract fees.

BERKSHIRE HATHAWAY INC.

Property, Plant and Equipment

Year ended October 2, 1965

Schedule V

| Classification | Balance at beginning of period | Additions at cost | Retirements or sales (1) | Balance at close of period |
|---|---|---|---|---|
| Land | $ 150,046 | - | 7,532 | 142,514 |
| Buildings | 4,578,329 | 7,683 | 153,500 | 4,432,512 |
| Machinery and equipment | 28,456,634 | 778,060 | 6,209,237 | 23,025,457 |
| Furniture and fixtures | 384,967 | 13,246 | 42,282 | 355,931 |
| Leasehold improvements | 15,825 | 10,423 | 2,819 | 23,429 |
| Motor vehicles | 49,752 | 2,400 | 12,253 | 39,899 |
| | $ 33,635,553 | 811,812 | 6,427,623 | 28,019,742 |

(1) Retirements and sales includes discontinued operations having a cost of $6,118,000 and a net book value of $3,264,000. The resulting loss from disposal of these assets amounting to $2,701,489 has been charged to the reserve for estimated loss on properties to be sold. See note 3 of notes to consolidated financial statements and Schedule XII.

BERKSHIRE HATHAWAY INC.

Accumulated Depreciation of Property, Plant and Equipment

Year ended October 2, 1965

Schedule VI

| Classification | Balance at beginning of period | Additions charged to profit and loss or income | Deductions Retirements, renewals and replacements (1) | Balance at close of period |
|---|---|---|---|---|
| Buildings | $ 3,191,762 | 80,942 | 134,141 | 3,138,563 |
| Machinery and equipment | 18,287,484 | 761,935 | 2,935,681 | 16,113,738 |
| Furniture and fixtures | 326,165 | 13,218 | 40,136 | 299,247 |
| Leasehold improvements | 2,999 | 4,170 | 704 | 6,465 |
| Motor vehicles | 45,279 | 2,159 | 12,288 | 35,150 |
| | $ 21,853,689 | 862,424 | 3,122,950 | 19,593,163 |

(1) See note to Schedule V.

BERKSHIRE HATHAWAY INC.

Reserves

Year ended October 2, 1965

Schedule XII

| | Balance at beginning of period | Additions charged to profit and loss or income | Deductions | Balance at end of period |
|---|---|---|---|---|
| Allowance for doubtful accounts | $ 245,354 | 120,000 | 85,052 (1) | 280,302 |
| Estimated loss on properties to be sold | 4,210,621 | 300,000 | 2,701,489 (2) | 1,809,132 |

(1) Accounts written off.

(2) Losses on sales of idle property and equipment. See Schedule V.