

Notes to Consolidated Financial Statements

FOR THE YEARS ENDED JUNE 29, 1997, JUNE 30, 1996 AND JULY 2, 1995

(1) Nature of Operations:

Briggs & Stratton Corporation (the Company) is a U.S. based producer of air cooled gasoline engines. These engines are sold primarily to original equipment manufacturers of lawn and garden equipment and other gasoline engine powered equipment worldwide.

(2) Summary of Significant Accounting Policies:

Fiscal Year: The Company's fiscal year consists of 52 or 53 weeks, ending on the Sunday nearest the last day of June in each year. Therefore, the 1997, 1996 and 1995 fiscal years were 52 weeks long. All references to years relate to fiscal years rather than calendar years.

Principles of Consolidation: The consolidated financial statements include the accounts of Briggs & Stratton Corporation and its wholly owned domestic and foreign subsidiaries after elimination of intercompany accounts and transactions.

Accounting Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents: This caption includes cash, commercial paper and certificates of deposit. The Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

Inventories: Inventories are stated at cost, which does not exceed market. The last-in, first-out (LIFO) method was used for determining the cost of approximately 93% of total inventories at June 29, 1997, June 30, 1996 and July 2, 1995. The cost for the remaining portion of the inventories was determined using the first-in, first-out (FIFO) method. If the FIFO inventory valuation method had been used exclusively, inventories would have been \$48,894,000, \$48,125,000 and \$43,582,000 higher in the respective years. The LIFO inventory

adjustment was determined on an overall basis, and accordingly, each class of inventory reflects an allocation based on the FIFO amounts.

Plant and Equipment and Depreciation:

Plant and equipment is stated at cost, and depreciation is computed using the straight-line method at rates based upon the estimated useful lives of the assets.

Expenditures for repairs and maintenance are charged to expense as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated. Upon retirement or disposition of plant and equipment, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in other income.

Income Taxes: The Provision for Income Taxes includes Federal, state and foreign income taxes currently payable and those deferred or prepaid because of temporary differences between financial statement and tax basis of assets and liabilities. The Future Income Tax Benefits represent temporary differences relating to current assets and current liabilities and the Deferred Income Tax Assets represent temporary differences relating to noncurrent assets and liabilities.

Research and Development Costs: Expenditures relating to the development of new products and processes, including significant improvements and refinements to existing products, are expensed as incurred. The amounts charged against income were \$19,525,000 in 1997, \$15,019,000 in 1996 and \$13,112,000 in 1995.

Accrued Employee Benefits: The Company's life insurance program includes payment of a death benefit to beneficiaries of retired employees. The Company accrues for the estimated cost of these benefits over the estimated working life of the employee. Past service costs for all retired employees have been fully provided for. The Company also accrues for the estimated cost of supplemental retirement and death benefit agreements with executive officers.

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Advertising Costs: Advertising costs, included in Engineering, Selling, General and Administrative Expenses on the accompanying Consolidated Statement of Earnings, are expensed as incurred. These expenses totaled \$7,989,000 in 1997, \$7,066,000 in 1996 and \$6,357,000 in 1995.

Foreign Currency Translation: Foreign currency balance sheet accounts are translated into United States dollars at the rates of exchange in effect at fiscal year end. Income and expenses are translated at the average rates of exchange in effect during the year. The related translation adjustments are made directly to a separate component of Shareholders' Investment.

Start-Up Costs: It is the Company's policy to expense all start-up costs for new manufacturing plants. Under this policy, the Company expensed \$11,660,000 in fiscal 1996 and \$5,300,000 in fiscal 1995.

Capitalized Software: This new balance sheet caption represents costs of software used in the Company's business. Amortization of Capitalized Software is computed on an item-by-item basis over a period of three to ten years, depending on the estimated useful life of the software. Accumulated amortization amounted to \$4,442,000 and \$3,367,000 as of June 29, 1997 and June 30, 1996, respectively. Capitalized Software on prior period balance sheets was reclassified from Prepaid Expense to the current caption.

Deferred Revenue on Sale of Plant & Equipment: The sale of the Company's Menomonee Falls, Wisconsin facility for approximately \$16.0 million was completed at the beginning of the fiscal quarter ended December 29, 1996. The provisions of the contract state that the Company will continue to own and occupy the warehouse portion of the facility for a period of up to ten years (the "Reservation Period"). The contract also contains a buyout clause, at the buyer's option and under certain circumstances, of the remaining Reservation Period.

Under the provisions of Statement of Financial Accounting Standards (FAS) No. 66, "Accounting for Sales of Real Estate," the Company is required to account for this as a financing transaction as the Company continues to have substantial involvement with the facility during the Reservation Period or until the buyout option is exercised. Under this method, the cash received is reflected as a deferred revenue, and the assets and the accumulated depreciation remain on the Company's books. Depreciation expense continues to be recorded each period, and imputed interest expense is also recorded and added to deferred revenue. Offsetting this is the imputed fair value lease income on the non-Company occupied portion of the building. A pretax gain, which will be recognized at the earlier of the exercise of the buyout option or the expiration of the Reservation Period, is estimated to be \$10 million to \$12 million. The annual cost of operating the warehouse portion of the facility is not material.

Derivatives: The Company uses derivative financial instruments to manage its foreign currency and interest rate exposures. Gains and losses relating to hedges of probable transactions with noncontrolled subsidiaries and third parties are deferred and recognized as adjustments of carrying amounts when the transaction occurs. Gains and losses on hedges of transactions that are not probable of occurring and hedges of transactions with controlled subsidiaries are recognized in the Company's results of operations.

Earnings Per Share: In February 1997, the Financial Accounting Standards Board issued FAS No. 128, "Earnings per Share." This statement establishes a new standard for computing and presenting earnings per share in financial statements. The Company will adopt the new standard in its fiscal 1998 second quarter financial statements. The impact of adoption of this standard will not be material to the Company's results of operations.

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Earnings per share of common stock are computed based on the weighted average number of shares outstanding during each period. The shares repurchased on May 20, 1997 pursuant to the dutch auction tender, which totaled 3,506,190 shares at \$51.00 per share, and the Company's ongoing share repurchase program, affect the year-to-date comparisons. Weighted average common shares outstanding for the quarter and year ended June 29, 1997 were 27,424,105 and 28,551,277, respectively, compared to 28,927,000 for each of the same periods in fiscal 1996.

(3) Income Taxes:

The provision for income taxes consists of the following (in thousands of dollars):

	<u>1997</u>	<u>1996</u>	<u>1995</u>
Current			
Federal	\$ 45,474	\$ 46,448	\$ 67,255
State	6,723	7,768	10,644
Foreign	1,648	1,654	873
	<u>53,845</u>	<u>55,870</u>	<u>78,772</u>
Deferred	(16,105)	770	(13,202)
Total	<u>\$ 37,740</u>	<u>\$ 56,640</u>	<u>\$ 65,570</u>

A reconciliation of the U.S. statutory tax rates to the effective tax rates follows:

	<u>1997</u>	<u>1996</u>	<u>1995</u>
U.S. statutory rate	35.0%	35.0%	35.0%
State taxes, net of			
Federal tax benefit	3.1%	3.4%	3.5%
Foreign Sales Corporation			
tax benefit	(.9%)	(.7%)	(.6%)
Other8%	.3%	.6%
Effective tax rate	<u>38.0%</u>	<u>38.0%</u>	<u>38.5%</u>

The components of deferred tax assets and liabilities at the end of the fiscal year were (in thousands of dollars):

	<u>1997</u>	<u>1996</u>
Future Income Tax Benefits:		
Inventory	\$ 2,916	\$ 2,518
Payroll related accruals	4,244	4,658
Warranty reserves	10,537	10,240
Other accrued liabilities	8,926	8,453
Miscellaneous	4,979	3,720
	<u>\$31,602</u>	<u>\$ 29,589</u>

	<u>1997</u>	<u>1996</u>
Deferred Income Taxes:		
Difference between book and		
tax methods applied to		
maintenance and supply		
inventories	\$12,464	\$ 9,982
Pension cost	9,688	(1,679)
Accumulated depreciation	(50,207)	(41,768)
Accrued employee benefits	7,904	7,232
Postretirement		
health care obligation	28,868	26,929
Deferred revenue on sale		
of plant & equipment	6,226	-
Miscellaneous	2,032	2,187
	<u>\$16,975</u>	<u>\$ 2,883</u>

The Company has not recorded deferred income taxes applicable to undistributed earnings of foreign subsidiaries that are indefinitely reinvested in foreign operations. These undistributed earnings amounted to approximately \$5,500,000 at June 29, 1997. If these earnings were remitted to the U.S., they would be subject to U.S. income tax. However, this tax would be substantially less than the U.S. statutory income tax because of available foreign tax credits.

(4) Industry Segments:

Certain information concerning the Company's industry segments is presented below (in thousands of dollars):

	<u>1995</u>
SALES -	
Engines & parts	\$1,276,264
Locks	63,413
	<u>\$1,339,677</u>
INCOME FROM OPERATIONS -	
Engines & parts	\$ 162,903
Locks	6,863
	<u>\$ 169,766</u>
DEPRECIATION EXPENSE -	
Engines & parts	\$ 42,746
Locks	1,699
	<u>\$ 44,445</u>
EXPENDITURES FOR PLANT AND EQUIPMENT -	
Engines & parts	\$ 124,604
Locks	6,430
	<u>\$ 131,034</u>

Notes . . .

On February 27, 1995, the Company spun off its lock business to its shareholders in a tax-free distribution. This spin-off was accomplished by distributing shares in a newly created corporation on the basis of one share in the new corporation for each five shares of Briggs & Stratton Corporation stock held on February 16, 1995. The newly created corporation, STRATTEC SECURITY CORPORATION, is publicly traded. This distribution resulted in a charge of \$40,966,000 against the retained earnings account and represented the total of the net assets transferred to STRATTEC. The financial statements of Briggs & Stratton Corporation have not been restated to deal with this distribution as a discontinued operation because the amounts were not material. Because of the spin-off, no industry segment data is being presented for fiscal 1997 or 1996.

Export sales for fiscal 1997 were \$304,230,000 (23% of total sales), for fiscal 1996 were \$323,747,000 (25%) and for fiscal 1995 were \$312,234,000 (23%). These sales were principally to customers in European countries.

In the fiscal years 1997, 1996 and 1995, there were sales to three major engine customers that exceeded 10% of total Company net sales. The sales to these customers are summarized below (in thousands of dollars and percent of total Company sales):

Customer	1997		1996		1995	
	Sales	%	Sales	%	Sales	%
A	\$282,428	21%	\$267,257	21%	\$237,241	18%
B	180,770	14%	177,314	14%	155,072	12%
C	142,840	11%	163,065	13%	189,916	14%
	<u>\$606,038</u>	<u>46%</u>	<u>\$607,636</u>	<u>48%</u>	<u>\$582,229</u>	<u>44%</u>

(5) Indebtedness:

The Company has access to a \$250,000,000 revolving credit facility (the Credit Facility) which expires in April 2002. The Company also has access to additional domestic lines of credit totaling \$13,000,000 which remain in effect until canceled by either party. They provide amounts for short-term use at the then prevailing rate. There are

no significant compensating balance requirements for any of these lines, and there were no borrowings at June 29, 1997 using these lines or the Credit Facility.

Borrowings under the Credit Facility by the Company bear interest at a rate per annum equal to, at its option, either:

- (1) the higher of (a) the bank's reference rate or (b) 0.5% per annum above the Federal Funds rate; or
- (2) LIBOR plus a margin that may be adjusted up or down based on the Company's debt ratings.

The Credit Facility contains certain restrictive covenants that require the Company to maintain certain financial conditions including a maximum limit on the ratio of debt to capital and a minimum fixed charge coverage ratio. The Credit Facility imposes limitations on liens, certain indebtedness, the sales of assets and certain investments.

The following data relates to domestic notes payable:

	1997	1996
Balance at		
Fiscal Year End	\$ 5,000,000	\$ 5,000,000
Weighted Average		
Interest Rate at		
Fiscal Year End	5.98%	6.10%

The lines of credit available to the Company in foreign countries are in connection with short-term borrowings and bank overdrafts used in the normal course of business. These amounts total \$17,200,000, expire at various times through June, 1998 and are renewable. None of these arrangements had material commitment fees or compensating balance requirements.

The following information relates to foreign loans:

	1997	1996
Balance at		
Fiscal Year End	\$13,359,000	\$14,922,000
Weighted Average		
Interest Rate at		
Fiscal Year End	4.49%	4.60%

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The Long-Term Debt caption consists of the following (in thousands of dollars):

	<u>1997</u>	<u>1996</u>
9.21% Senior Notes Due 2001 at Face Amount	\$ 60,000	\$ 75,000
7.25% Notes Due 2007, Net of Unamortized Discount of \$2,103 in 1997	<u>97,897</u>	<u>—</u>
	<u>\$157,897</u>	<u>\$ 75,000</u>
Less Current Maturities	<u>\$ 15,000</u>	<u>\$ 15,000</u>
Total Long-Term Debt	<u>\$142,897</u>	<u>\$ 60,000</u>

The 9.21% Senior Notes are due June 15, 2001. Payments on these notes are due in five equal annual installments beginning in 1997. The notes include covenants that limit total borrowings, require maintenance of a minimum net worth and set certain restrictions on the sale or collateralizing of the Company's assets.

The 7.25% notes are due September 15, 2007. No principal payments are due before that date. These notes have covenants that limit secured funded debt and certain sale-leaseback transactions.

(6) Other Income:

The components of other income (expense) are (in thousands of dollars):

	<u>1997</u>	<u>1996</u>	<u>1995</u>
Interest income	\$ 3,981	\$ 4,477	\$ 6,840
Loss on the disposition of plant and equipment	<u>(1,608)</u>	<u>(2,692)</u>	<u>(1,452)</u>
Income from joint ventures	<u>3,026</u>	<u>2,957</u>	<u>2,842</u>
Other items	<u>67</u>	<u>970</u>	<u>959</u>
Total	<u>\$ 5,466</u>	<u>\$ 5,712</u>	<u>\$ 9,189</u>

(7) Commitments and Contingencies:

The Company is a 50% guarantor on bank loans of two unconsolidated joint ventures. One is in Japan for the manufacture of engines and the second in the United States for the manufacture of parts. These bank loans totaled approximately \$8,000,000 at the end of 1997.

Product and general liability claims arise against the Company from time to time in the ordinary course of business. The Company is self-insured for future claims up to \$1 million per claim. Accordingly, a reserve is maintained for the estimated costs of such claims. At June 29, 1997 and June 30, 1996, the reserve for product and general liability claims was \$4.6 million and \$6.5 million, respectively, based on available information. There is inherent uncertainty as to the eventual resolution of unsettled claims. Management, however, believes that any losses in excess of established reserves will not have a material effect on the Company's financial position or results of operations.

The Company has no material commitments for materials or capital expenditures at June 29, 1997.

(8) Stock Options:

The Company has a Stock Incentive Plan under which 3,361,935 shares of common stock have been reserved for issuance. The Company accounts for the plan under Accounting Principles Board No. 25, under which no compensation cost has been recognized. Had compensation cost for these plans been determined consistent with FAS No. 123, "Accounting for Stock-Based Compensation," the Company's net income and earnings per share would have been reduced to the following pro forma amounts:

	<u>1997</u>	<u>1996</u>
Net Income (in thousands):		
As Reported	\$61,565	\$92,412
Pro Forma	<u>\$60,777</u>	<u>\$91,690</u>
Earnings Per Share:		
As Reported	\$2.16	\$3.19
Pro Forma	<u>\$2.13</u>	<u>\$3.17</u>

Because the FAS No. 123 method of accounting has not been applied to options granted prior to July 2, 1995, the resulting pro forma compensation cost may not be representative of that to be expected in future years.

Notes . . .

Information on the options outstanding is as follows:

		1997	
		Shares	Wtd. Avg. Ex. Price
Balance, beginning of year	1,704,531		\$ 42.98
Granted during the year	106,550		53.30
Exercised during the year	(24,369)		17.26
Balance, end of year	<u>1,786,712</u>		<u>\$ 43.95</u>
		1996	
		Shares	Wtd. Avg. Ex. Price
Balance, beginning of year	1,169,620		\$ 38.41
Granted during the year	600,000		49.08
Exercised during the year	(65,089)		17.07
Balance, end of year	<u>1,704,531</u>		<u>\$ 42.98</u>
		1995	
		Shares	Wtd. Avg. Ex. Price
Balance, beginning of year	606,864		\$ 32.76
Granted during the year	552,000		45.85
Increase due to spin-off	83,843		38.08
Exercised during the year	(43,827)		15.91
Terminated during the year	(29,260)		49.77
Balance, end of year	<u>1,169,620</u>		<u>\$ 38.41</u>

Grant Summary

Fiscal Year	Grant Date	Exercise Price (a)	Date Exercisable	Options Outstanding	Expiration Date
1990	2-20-90	\$13.014	50%, 1-1-94; 50%, 1-1-95	3,782	2-19-00
1991	2-19-91	14.524	50%, 1-1-95; 50%, 1-1-96	79,405	2-18-01
1992	5-18-92	21.525	50%, 1-1-96; 50%, 1-1-97	171,385	5-17-02
1994	8-16-93	48.369	8-16-96	258,085	8-16-98
1995	8-12-94	45.854	8-12-97	567,505	8-12-99
1996	8-7-95	49.080	8-7-98	600,000	8-7-00
1997	8-6-96	53.300	8-6-99	106,550	8-6-01

There were no options granted in fiscal 1993.

- (a) Exercise prices have been adjusted as appropriate to reflect a two-for-one stock split and the spin-off of the Company's lock business.

The grant-date fair market value of the options granted in fiscal 1997 and 1996 was \$5.42 and \$5.39, respectively. The fair value of each option is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for the 1997 and 1996 option grants, respectively: risk free interest rates of 6.25% and 6.36%; expected volatility of 20.6% and

24.6%; expected dividend yields of 2.5% and 2.7%; and expected lives of the options of 5 years.

(9) Shareholder Rights Plan:

On August 6, 1996, the Board of Directors declared a dividend distribution of one common stock purchase right (a "right") for each share of the Company's common stock outstanding on August 19, 1996. Each right would entitle shareowners to buy one-half of one share of the Company's common stock at an exercise price of \$160.00 per full common share, subject to adjustment. The rights are not currently exercisable, but would become exercisable if certain events occurred relating to a person or group acquiring or attempting to acquire 15 percent or more of the outstanding shares of common stock. The rights expire on August 19, 2006, unless redeemed or exchanged by the Company earlier. Rights granted under a previous plan expired July 1, 1996.

(10) Foreign Exchange Risk Management:

The Company enters into forward exchange contracts to hedge purchase commitments denominated in foreign currencies. The term of these currency derivatives never exceeds one year and the purpose is to protect the Company from the risk that the eventual dollars being transferred will be adversely affected by changes in exchange rates.

The Company has forward foreign currency exchange contracts to purchase 5.5 billion Japanese yen for \$46 million through June, 1998. These contracts are used to hedge the commitments to purchase engines from the Company's Japanese joint venture and accordingly any gain or loss has been deferred at the end of the 1997 fiscal year. The amount deferred was a gain of approximately \$2.5 million.

The Company's foreign subsidiaries have the following forward currency contracts outstanding at the end of fiscal 1997:

Currency	In Millions		Latest Expiration Date
	Local Currency	U.S. Dollars	
German Deutschemarks6	.2	July, 1997
Canadian Dollars7	.5	July, 1997
Australian Dollars	1.3	1.0	September, 1997

There are no significant gains or losses included in the above amounts.

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(11) Employee Benefit Costs:

Retirement Plan

The Company has noncontributory, defined benefit retirement plans covering most Wisconsin employees. The following tables summarize the plans' income and expense, actuarial assumptions, and funded status for the three years indicated (dollars in thousands):

	Qualified Plans			Supplemental Plans		
	1997	1996	1995	1997	1996	1995
<u>Income and Expense:</u>						
Service Cost-Benefits Earned						
During the Year	\$ 11,309	\$ 13,143	\$ 15,098	\$ 378	\$ 456	\$ 453
Interest Cost on Projected						
Benefit Obligation	40,990	41,722	39,877	860	926	904
Actual Return on Plan Assets	(114,303)	(104,872)	(89,941)	(11)	(9)	(3)
Net Amortization, Deferral						
and Windows	58,525	51,830	37,078	395	462	333
Net Periodic Pension						
Expense (Income)	\$ (3,479)	\$ 1,823	\$ 2,112	\$ 1,622	\$ 1,835	\$ 1,687
<u>Actuarial Assumptions:</u>						
Discount Rate Used to Determine						
Present Value of Projected						
Benefit Obligation	7.75%	7.75%	7.75%	7.75%	7.75%	7.75%
Expected Rate of Future						
Compensation Level Increases	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%
Expected Long-Term Rate of						
Return on Plan Assets	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%
<u>Funded Status:</u>						
Actuarial Present Value of						
Benefit Obligations:						
Vested	\$ 482,712	\$ 413,035	\$ 389,117	\$ 8,869	\$ 8,286	\$ 7,991
Non-Vested	32,735	34,268	36,144	—	21	6
Accumulated Benefit						
Obligation	515,447	447,303	425,261	8,869	8,307	7,997
Effect of Projected Future						
Wage and Salary Increases	82,941	120,083	124,651	3,228	4,766	4,679
Projected Benefit Obligation	598,388	567,386	549,912	12,097	13,073	12,676
Plan Assets at Fair Market Value	767,108	681,819	609,385	127	126	100
Plan Assets in Excess of (Less Than)						
Projected Benefit Obligation	168,720	114,433	59,473	(11,970)	(12,947)	(12,576)
Remaining Unrecognized Net						
Obligation (Asset) Arising						
from the Initial Application of						
SFAS No. 87	(26,006)	(31,321)	(36,902)	132	179	258
Unrecognized Net Loss (Gain)	(164,779)	(75,983)	(21,992)	2,531	4,494	5,277
Unrecognized Prior Service Cost	(2,002)	(2,447)	(2,185)	953	1,029	1,102
Prepaid (Accrued) Pension Cost	\$ (24,067)	\$ 4,682	\$ (1,606)	\$ (8,354)	\$ (7,245)	\$ (5,939)
Less Current Portion	—	—	—	530	511	511
	<u>\$ (24,067)</u>	<u>\$ 4,682</u>	<u>\$ (1,606)</u>	<u>\$ (7,824)</u>	<u>\$ (6,734)</u>	<u>\$ (5,428)</u>

Notes . . .

The Company offered early retirement windows to certain of its Milwaukee union members during the 1995 fiscal year. As a result, \$13,806,000 was added to pension expense and \$5,253,000 was added to postretirement health care expense in the fourth quarter of the 1995 fiscal year. When the retirements were scheduled to occur in the first fiscal quarter of 1996, a number of these union members canceled their acceptance, and thus credits totaling \$3,477,000 were recorded as a change in the original accounting estimate. A second retirement window was offered in fiscal 1997. The cost of this window was additional pension expense of \$33,457,000 and additional postretirement health care expense of \$3,644,000 in the fourth quarter of the 1997 fiscal year.

During fiscal 1996, the defined benefit pension plan which covered employees at two of the Company's plants was terminated and replaced by a defined contribution retirement plan that includes most U.S. non-Wisconsin employees. The impact of the termination was not material. Under the new plan, the Company will make a contribution on behalf of covered employees equal to 2% of each participant's gross income, as defined. For fiscal 1997 and 1996, the cost to the Company was \$1,352,000 and \$757,000, respectively.

Most U.S. employees of the Company may participate in a salary reduction deferred compensation retirement plan. The Company makes matching contributions of \$.50 for every \$1.00 deferred by a participant to a maximum of 1-1/2% or 3% of each participant's salary, depending upon the participant's group. Company contributions totaled \$3,944,000 in 1997, \$2,825,000 in 1996 and \$1,756,000 in 1995.

Postretirement Benefits

The Company records the expected health care and life insurance benefits for employees during the years that the employees render service.

For measurement purposes, a 10.5% annual rate of increase in the per capita cost of covered health care claims was assumed for the years 1995 through

1997, decreasing gradually to 6% for the year 2007. The health care cost trend rate assumption has a significant effect on the amounts reported. The rates, if changed by one percentage point, would change the accumulated postretirement benefit by \$5,472,000 and would change the service and interest cost by \$641,000 for the year.

The discount rate used in determining the accumulated postretirement benefit obligations was 7.75% compounded annually. Both the health care and life insurance plans are unfunded.

The components of the accumulated postretirement benefit obligations were (in thousands of dollars):

	<u>Health Care</u>	
	<u>1997</u>	1996
Retirees	\$51,553	\$33,044
Fully eligible plan participants	467	4,077
Other active participants	26,961	32,628
	<u>\$78,981</u>	<u>\$69,749</u>
Unrecognized gain (loss)	(161)	4,000
	<u>\$78,820</u>	<u>\$73,749</u>
Less current portion	4,800	4,700
	<u>\$74,020</u>	<u>\$69,049</u>
	<u>Life Insurance</u>	
	<u>1997</u>	1996
Retirees	\$ 9,048	\$ 8,840
Fully eligible plan participants	1,720	2,226
Other active participants	1,453	1,736
	<u>\$12,221</u>	<u>\$12,802</u>
Unrecognized net obligation	(507)	(553)
Unrecognized prior service cost	(827)	(898)
Unrecognized loss	(35)	(908)
	<u>\$10,852</u>	<u>\$10,443</u>
Less current portion	-	-
	<u>\$10,852</u>	<u>\$10,443</u>

The current portion of the health care component above represents the benefits expected to be paid within the next twelve months and is included in the caption Accrued Liabilities in the accompanying balance sheet. The net health care balance has its own caption in this balance sheet. The life insurance component is included in the caption Accrued Employee Benefits.

Notes . . .

The net periodic postretirement costs recorded were (in thousands of dollars):

	<u>Health Care</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
Service cost-benefits attributed to service during the year	\$1,272	\$1,596	\$1,680
Interest cost on accumulated benefit obligation	5,226	5,480	5,150
Other	<u>—</u>	<u>(91)</u>	<u>—</u>
	<u>\$6,498</u>	<u>\$6,985</u>	<u>\$6,830</u>
	<u>Life Insurance</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
Service cost-benefits attributed to service during the year	\$ 87	\$ 90	\$ 73
Interest cost on accumulated benefit obligation	964	947	801
Other	118	118	47
	<u>\$1,169</u>	<u>\$1,155</u>	<u>\$ 921</u>

Postemployment Benefits

The Company also accrues the expected cost of postemployment benefits over the years that the employees render service. These benefits are substantially smaller amounts because they apply only to employees who permanently terminate employment prior to retirement. The items included in this amount are disability payments, life insurance and medical benefits, and these amounts are also discounted using a 7.75% interest rate.

The balance in this reserve at the end of fiscal 1997 was \$1,468,000 and at the end of fiscal 1996 was \$1,245,000. Both were included in the caption Accrued Employee Benefits in the accompanying balance sheets.

(12) Disclosures about Fair Value of Financial Instruments:

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and Cash Equivalents, Domestic Notes Payable and Foreign Loans: The carrying amount approximates fair value because of the short maturity of those instruments.

Long-Term Debt: The fair value of the Company's long-term debt is estimated based on quotations made on similar issues.

The estimated fair values of the Company's financial instruments are as follows (in thousands of dollars):

	<u>1997</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>
Cash and cash equivalents	\$ 112,859	\$ 112,859
Domestic notes payable	\$ 5,000	\$ 5,000
Foreign loans	\$ 13,359	\$ 13,359
Long-term debt –		
9.21% Senior Notes due 2001, including current maturities . .	\$ 60,000	\$ 62,885
7.25% Notes due 2007	\$ 97,897	\$ 100,531
	<u>1996</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>
Cash and cash equivalents	\$ 150,639	\$ 150,639
Domestic notes payable	\$ 5,000	\$ 5,000
Foreign loans	\$ 14,922	\$ 14,922
Long-term debt –		
9.21% Senior Notes due 2001, including current maturities . .	\$ 75,000	\$ 77,365