FINJAN HOLDINGS, INC.
Form 10-Q
May 08, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 31, 2014

or

¨ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from __________ to __________

Commission File Number: 001-33304

FINJAN HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-4075963**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

122 East 42nd Street

New York, New York,

(646) 755-3320

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of May 7, 2014, 22,368,453 shares of the registrant s common stock, par value $0.0001 per share, were outstanding.

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FINJAN HOLDINGS, INC.

QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTER ENDED MARCH 31, 2014

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

FINJAN HOLDINGS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	March 31, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$ 23,549	$ 24,598
Accounts receivable, net	51	50
Inventories	61	34
Prepaid expenses and other current assets	214	150
Total current assets	23,875	24,832
Property and equipment, net	958	953
Intangible assets, net	1,253	1,333
Goodwill	306	306
Investments	500	500
Other non-current assets	23	23
Total Assets	$ 26,915	$ 27,947
Liabilities and Stockholders Equity		
Current Liabilities:		
Accounts payable	$ 873	$ 495
Accounts payable related parties	19	15
Accrued expenses	591	336
Accrued income taxes	5	4
Other current liabilities	32	35
Total current liabilities	1,520	885
Deferred tax liabilities	37	39
Total Liabilities	$ 1,557	$ 924
Commitments and contingencies		

Stockholders Equity				
Preferred stock $0.0001 par value; 10,000,000 shares authorized; no shares issued and outstanding at March 31, 2014 and December 31, 2013				
Common stock $0.0001 par value; 1,000,000,000 shares authorized; 22,368,453 shares issued and outstanding at March 31, 2014 and December 31, 2013		2		2
Additional paid-in capital		21,884		21,546
Retained earnings		3,472		5,475
Total Stockholders Equity		25,358		27,023
Total Liabilities and Stockholders Equity	$	26,915	$	27,947

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FINJAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except share and per share data)

(Unaudited)

	For the Three Months Ended March 31,	
	2014	**2013**
Revenues	$ 175	$
Cost of revenues	134	
Gross profit	41	
Operating Expenses:		
Selling, general and administrative	3,123	847
Total operating expenses	3,123	847
Loss from operations	(3,082)	(847)
Other Income		
Gain on settlements	1,000	
Other income	12	
Interest income	68	80
Total other income	1,080	80
Loss before provision for income taxes	(2,002)	(767)
Provision for income taxes	1	
Net Loss	$ (2,003)	$ (767)
Net Loss Per Share:		
Basic and Diluted	$ (0.09)	$ (0.04)
Weighted Average Number of Common Shares Outstanding:		
Basic and Diluted	22,368,453	20,590,596

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FINJAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2014	**2013**
Cash Flows From Operating Activities		
Net Loss	$ (2,003)	$ (767)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	132	
Stock-based compensation expense	338	
Deferred tax liability	(2)	
Changes in operating assets and (liabilities):		
Accounts receivable	(1)	
Inventories	(27)	
Prepaid expenses and other current assets	(64)	
Accrued expenses	240	
Accounts payable	378	(2,159)
Accounts payable related parties	4	
Other current liabilities	(3)	
Accrued income taxes	1	(25,325)
Total Adjustments	996	(27,484)
Net Cash Used in Operating Activities	(1,007)	(28,251)
Cash Flows From Investing Activities		
Purchases of property and equipment	(42)	
Net Cash Used in Investing Activities	(42)	
Cash Flows From Financing Activities		
Repayment of loan from former parent		(33,943)
Net Cash Used in Financing Activities		(33,943)
Net Decrease in Cash and Cash Equivalents	(1,049)	(62,194)
Cash and Cash Equivalents Beginning	24,598	91,545

Cash and Cash Equivalents Ending	$ 23,549	$ 29,351
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the quarter for:		
Income taxes	$	$ 25,325
Non-cash Investing and Financing activities:		
Purchase of property and equipment in exchange for finance agreement	$ 15	$
Dividend of investments to parent	$	$ 12,784

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FINJAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

NOTE 1 THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Finjan Holdings, Inc. (the Company , or Finjan Holdings), a Delaware corporation (formerly Converted Organics, Inc.), has two reportable business segments: a web and network security technology segment focused on licensing and enforcing its technology patent portfolio, operated by its wholly-owned subsidiary Finjan, Inc. (Finjan), and an organic fertilizer segment operated by another wholly-owned subsidiary, Converted Organics of California, LLC (Converted Organics).

On June 3, 2013, Converted Organics, Inc. entered into an Agreement and Plan of Merger (the Merger Agreement) with Finjan. Effective June 3, 2013 and pursuant to the Merger Agreement, a wholly owned subsidiary merged with and into Finjan and Finjan became a wholly-owned subsidiary of Converted Organics, Inc. (the Merger). The transaction was accounted for as a reverse acquisition under the acquisition method of accounting for business combinations, with Finjan being treated as the acquiring company in the Merger for accounting purposes. Accordingly, the assets and liabilities and the historical operations that are reflected in Finjan Holdings condensed consolidated financial statements are those of Finjan and are recorded at the historical cost basis of Finjan. The results of operations of the acquired Converted Organics business have been included in the condensed consolidated statement of operations since the date of Merger.

Unless otherwise indicated or the context otherwise requires, references to Finjan Holdings, or the Company refer to Finjan Holdings, Inc., and its consolidated subsidiaries. Disclosures relating to the pre-merger business of Finjan Holdings, Inc., unless noted as being the business of Converted Organics prior to the Merger, pertain to the business of Finjan prior to the Merger.

BASIS OF PRESENTATION

These unaudited condensed consolidated financial statements have been prepared following the requirements of the Securities and Exchange Commission, or SEC , for interim reporting. As permitted under those rules, certain footnotes and other financial information that are normally required by U.S. GAAP, can be condensed or omitted. The information included in this quarterly report on Form 10-Q should be read in conjunction with the consolidated financial statements and notes thereto of the Company for the year ended December 31, 2013 which were included in the Annual Report on Form 10-K filed by the Company on March 14, 2014.

In the opinion of management, these condensed consolidated financial statements have been prepared on the same basis as the annual consolidated financial statements and notes thereto of the Company and include all adjustments, consisting only of normal recurring adjustments, considered necessary for the fair presentation of the Company s financial position and operating results. The results for the three months ended March 31, 2014 and 2013 are not necessarily indicative of the operating results for the year ending December 31, 2014, for any other interim period or for any future period.

USE OF ESTIMATES

The preparation of financial statements in conformity with U.S. GAAP 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. On an ongoing basis, the Company evaluates its estimates, including those related to stock-based compensation expense, impairment of intangible assets, the determination of the economic useful life of property and equipment and intangible assets, income taxes and valuation allowances against net deferred tax assets, and the application of the acquisition method of accounting for business combinations. Management bases its estimates on historical experience or on various other assumptions that it believes to be reasonable under the circumstances. Actual results could differ from those estimates.

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FINJAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Principles of Consolidation

The accompanying condensed consolidated financial statements include the accounts of Finjan Holdings and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Concentrations of Credit Risk

The Company maintains its cash and cash equivalents in financial institutions located in the United States. At times, the Company s cash and cash equivalent balances may be uninsured or in deposit accounts that exceed the Federal Deposit Insurance Corporation (FDIC) insurance limits. The Company has not experienced any losses in such accounts. As of March 31, 2014 and December 31, 2013, substantially all of the company s cash and cash equivalents are uninsured.

During the three months ended March 31, 2014 approximately 12%, 22% and 29% of the revenues generated by the company were from three customers. The Company did not have revenue during the comparable period in 2013.

Net Income (Loss) per Common Share

Basic net income (loss) per common share is based upon the weighted-average number of common shares outstanding. Diluted net income (loss) per common share is based on the weighted-average number of common share outstanding and potentially dilutive common shares outstanding.

Potentially dilutive common shares from employee equity plans and warrants are determined by applying the treasury stock method to the assumed exercise of warrants and share options and are excluded from the computation of diluted net loss per share because their inclusion would be anti-dilutive and consist of the following:

	March 31, 2014	December 31, 2013
Options	1,625,476	1,625,476
Warrants*		
Total	1,625,476	1,625,476

* Warrants are currently exercisable for less than one share of common stock, and therefore anti-dilutive, as a result of the 1-for-10 reverse stock split that the Company effected on November 8, 2011, the 1-for-500

reverse stock split that the Company effected on March 5, 2012, the 1-for-500 reverse stock split that the Company effected on June 3, 2013 and the 1-for-12 reverse stock split the Company effected on August 22, 2013. The warrants are subject to further adjustments in the future, which may have the effect of increasing or decreasing the exercise price and the number of shares issuable upon exercise of the warrants.

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FINJAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Recently Issued Accounting Pronouncements Not Yet Adopted

The Company has determined there are no new accounting standards that are expected to have a material impact on the Company s condensed consolidated financial statements.

Subsequent Events

Management has evaluated subsequent events or transactions occurring through the date on which the financial statements were issued. See note 9.

Note 2 Pro-forma Financial Information

As described in Note 1, the Company completed the Merger on June 3, 2013. The following unaudited pro forma information presents the combined results of operations for the three months ended March 31, 2013 as if the merger with Converted Organics, Inc. had been completed on January 1, 2013. The pro forma financial information includes adjustments to reflect one time charges and amortization of fair value adjustments in the appropriate pro forma periods as though the companies were combined as of the beginning of 2013. These adjustments include:

An increase in depreciation and amortization expense of $3,000 for the three months ended March 31, 2013 related to property and equipment and the fair value of acquired identifiable assets.

The unaudited pro forma results do not reflect operating efficiencies or potential cost savings which may be implemented after the Merger:

	Three Months Ended March 31, (In thousands, except share and per share data) 2013
Revenue	$ 400
Net loss	$ (2,453)

Net loss per common share, basic and diluted	$	(0.12)
Weighted average shares outstanding:		
Basic and diluted		20,590,596

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FINJAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

NOTE 3 BALANCE SHEET COMPONENTS

INVENTORIES

The components of inventory were as follows:

	March 31, 2014	December 31, 2013
	(In thousands)	
Raw materials	$ 36	$ 13
Finished goods	25	21
Inventory	$ 61	$ 34

ACCRUED EXPENSES

The components of accrued expenses were as follows:

	March 31, 2014	December 31, 2013
	(In thousands)	
Legal	$ 396	$ 238
Compensation	180	78
Professional fees		20
Other	15	
Accrued expenses	$ 591	$ 336

NOTE 4 COMMITMENTS

OPERATING LEASES

The Company leases a production facility in California. Under the terms of the lease, the Company owes minimum annual rent of $125,202, payable in monthly installments of $10,433, unless earlier terminated in accordance with the lease. The annual rental rate is subject to increase on each annual anniversary of the commencement of the immediately preceding rental year by 3% of the rent paid during the immediately preceding year. This lease expires in

2018.

On September 9, 2013, the Company entered into a lease for its new corporate headquarters for a period of five years beginning October 1, 2013. Under the terms of the lease, the Company owes an initial annual rent of $138,952, payable in monthly installments of $11,579, unless earlier terminated in accordance with the lease. The annual rental rate is subject to an increase on a cumulative basis after the first lease year at the rate of 2.5% per annum compounded annually.

On March 20, 2014, the Company received the consent of the master landlord for a sublease agreement dated March 10, 2014, pursuant to which the Company subleased office space in Menlo Park, California. From the commencement date through November 30, 2017, the Company owes an initial annual rent of $164,619, payable in equal monthly installments, unless earlier terminated by either party in accordance with the lease. The annual rental rate is subject to an approximately 3.0% increase at each anniversary of the commencement date during the term.

The following table sets forth the Company s aggregate future minimum payments under its operating lease commitments as of March 31, 2014 (in thousands):

Year ending December 31,	
2014	$ 312
2015	445
2016	457
2017	448

2 years later	39,456	42,468	40,456	46,916	47,293	47,636	49,960	53,600	53,961	
3 years later	39,608	41,645	40,350	45,902	45,675	46,793	49,143	52,526		
4 years later	38,971	41,676	39,198	44,665	45,337	46,099	48,262			
5 years later	39,317	40,884	38,003	44,618	44,914	45,630				
6 years later	38,804	39,888	37,946	44,406	44,659					
7 years later	38,060	40,008	37,631	44,355						
8 years later	38,280	39,796	37,192							
9 years later	38,189	39,472								
10 years later	37,943									
Cumulative deficiency (redundancy)	(2,144)	(3,362)	(5,587)	(4,521)	(4,828)	(6,907)	(5,268)	(4,201)	(3,255)	(2,031)
Cumulative foreign exchange effect*	618	85	540	961	381	590	361	280	461	666
Net deficiency (redundancy)	$ (1,526)	$ (3,277)	$ (5,047)	$ (3,560)	$ (4,447)	$ (6,317)	$ (4,907)	$ (3,921)	$ (2,794)	$ (1,365)
Deferred charge changes and reserve discounts	2,726	2,591	2,157	1,970	1,806	1,698	989	645	306	128
Deficiency (redundancy) before deferred charges and reserve discounts	$ (4,252)	$ (5,868)	$ (7,204)	$ (5,530)	$ (6,253)	$ (8,015)	$ (5,896)	$ (4,566)	$ (3,100)	$ (1,493)
Cumulative payments:										
1 year later	$ 7,793	$ 9,345	$ 8,865	$ 8,486	$ 8,315	$ 9,191	$ 8,854	$ 10,628	$ 10,978	$ 11,381
2 years later	12,666	15,228	13,581	13,394	13,999	14,265	14,593	17,260	17,827	
3 years later	16,463	18,689	16,634	17,557	16,900	17,952	18,300	21,747		
4 years later	18,921	20,890	19,724	19,608	19,478	20,907	22,008			

5 years later	20,650	23,507	21,143	21,660	21,786	22,896
6 years later	22,865	24,935	22,678	23,595	23,339	
7 years later	24,232	26,266	23,892	24,807		
8 years later	25,430	26,928	24,831			
9 years later	26,624	28,031				
10 years later	26,917					

* The amounts of re-estimated liabilities in the table above related to these operations are based on the applicable foreign currency exchange rates as of the end of the re-estimation period. The cumulative foreign exchange effect represents the cumulative effect of changes in foreign exchange rates from the original balance sheet date to the end of the re-estimation period.

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The first section of the table reconciles the estimated liability for unpaid losses and loss adjustment expenses recorded at the balance sheet date for each of the indicated years from the liability reflected in Berkshire s Consolidated Balance Sheet to the net amount, after reductions for amounts recoverable under ceded reinsurance, deferred charges on retroactive reinsurance contracts and loss reserve discounts.

Certain workers compensation loss liabilities are discounted for both statutory and GAAP reporting purposes at an interest rate of 4.5% per annum for claims occurring before 2003 and at 1% per annum for claims occurring thereafter. In addition, deferred charges are recorded as assets at the inception of retroactive reinsurance contracts for the excess, if any, of the estimated ultimate unpaid losses and loss adjustment expenses over the premiums received. The deferred charges are subsequently amortized over the expected claim payment period. Deferred charge amortization and loss reserve discount accretion are recorded as components of insurance losses and loss adjustment expenses incurred.

The second section of the table shows the re-estimated net unpaid losses, including the impact of changes in related reserve discount accretion and deferred charge amortization, based on experience as of the end of each succeeding year. The re-estimated amount also reflects the effect of loss payments and re-estimation of remaining ultimate unpaid liabilities. The line labeled cumulative deficiency (redundancy) represents the aggregate increase (decrease) in the initial estimates from the original balance sheet date through December 31, 2014. These amounts have been reported in earnings over time as components of losses and loss adjustment expenses and include accumulated reserve discount accretion and deferred charge amortization. Due to the significance of the deferred charges and reserve discounts, the cumulative changes in such balances that are included in the cumulative deficiency/redundancy amounts are also provided.

The redundancies or deficiencies shown in each column should be viewed independently of the other columns because redundancies or deficiencies arising in earlier years are included as components of redundancies or deficiencies in the more recent years. Liabilities assumed under retroactive reinsurance contracts are treated as occurrences in the year the policy incepted, as opposed to when the underlying losses actually occurred, which is prior to the policy inception date.

The third part of the table shows the cumulative amount of net losses and loss adjustment expenses paid with respect to recorded net liabilities as of the end of each succeeding year. While the information in the table provides a historical perspective on the adequacy of unpaid losses and loss adjustment expenses established in previous years, and of the subsequent payments of claims, it should not be assumed that historical experience will continue in the future.

Investments Invested assets of insurance businesses derive from shareholder capital as well as funds provided from policyholders through insurance and reinsurance business (float). Float is an approximation of the amount of net policyholder funds available for investment. That term denotes the sum of unpaid losses and loss adjustment expenses, life, annuity and health benefit liabilities, unearned premiums and other policyholder liabilities less the sum of premium balances receivable, losses recoverable from reinsurance ceded, deferred policy acquisition costs, deferred charges on reinsurance contracts and related deferred income taxes. On a consolidated basis, the amount of float has grown from approximately $63 billion at the end of 2009 to approximately $84 billion at the end of 2014, primarily through internal growth. BHRG and General Re accounted for approximately 74% of the consolidated float as of December 31, 2014. Equally important as the amount of the float is its cost, represented by Berkshire s periodic net underwriting gain or loss. The increases in the amount of float plus the substantial amounts of shareholder capital devoted to insurance and reinsurance activities have generated meaningful increases in the levels of investments and investment income over the past five years.

Investment portfolios of insurance subsidiaries include ownership of equity securities of other publicly traded companies which are concentrated in relatively few companies and relatively large amounts of fixed maturity securities and cash and cash equivalents. Fixed maturity investments consist of obligations of the U.S. Government, U.S. states and municipalities, mortgage-backed securities issued primarily by the three major U.S. Government and Government-sponsored agencies, as well as obligations of foreign governments and corporate obligations. Investment portfolios are primarily managed by Berkshire s corporate office. Generally, there are no targeted investment allocation rates established by management with respect to investment activities. However, investment portfolios have historically included a greater proportion of equity investments than is customary in the insurance industry. Management may increase or decrease investments in response to perceived changes in opportunities for income or price appreciation relative to risks associated with the issuers of the securities.

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Railroad Business

On February 12, 2010, Berkshire completed its acquisition of Burlington Northern Santa Fe Corporation through the merger of a wholly-owned merger subsidiary and Burlington Northern Santa Fe Corporation. The merger subsidiary was the surviving entity and was renamed Burlington Northern Santa Fe, LLC (BNSF). BNSF is based in Fort Worth, Texas, and through BNSF Railway Company operates one of the largest railroad systems in North America with approximately 32,500 route miles of track (excluding multiple main tracks, yard tracks and sidings) in 28 states, and also operates in three Canadian provinces. BNSF Railway owns approximately 23,000 route miles, including easements, and operates on approximately 9,500 route miles of trackage rights that permit BNSF Railway to operate its trains with its crews over other railroads tracks. As of December 31, 2014, the total BNSF Railway system, including single and multiple main tracks, yard tracks and sidings, consisted of approximately 51,000 operated miles of track, all of which are owned by or held under easement by BNSF Railway, except for approximately 10,500 miles operated under trackage rights. BNSF had approximately 48,000 employees at the end of 2014.

In serving the Midwest, Pacific Northwest, Western, Southwestern and Southeastern regions and ports of the country, BNSF transports a range of products and commodities derived from manufacturing, agricultural and natural resource industries. Over half of the freight revenues of BNSF are covered by contractual agreements of varying durations, while the balance is subject to common carrier published prices or quotations offered by BNSF. BNSF s financial performance is influenced by, among other things, general and industry economic conditions at the international, national and regional levels. BNSF s primary routes, including trackage rights, allow it to access major cities and ports in the western and southern United States as well as parts of Canada and Mexico. In addition to major cities and ports, BNSF efficiently serves many smaller markets by working closely with approximately 200 shortline partners. BNSF has also entered into marketing agreements with other rail carriers, expanding the marketing reach for each railroad and their customers. For the year ending December 31, 2014, approximately 31% of freight revenues were derived from consumer products, 28% from industrial products, 22% from coal and 19% from agricultural products.

Regulatory Matters

BNSF is subject to federal, state and local laws and regulations generally applicable to all of its businesses. Rail operations are subject to the regulatory jurisdiction of the Surface Transportation Board (STB) of the United States Department of Transportation (DOT), the Federal Railroad Administration of the DOT, the Occupational Safety and Health Administration (OSHA), as well as other federal and state regulatory agencies and Canadian regulatory agencies for operations in Canada. The STB has jurisdiction over disputes and complaints involving certain rates, routes and services, the sale or abandonment of rail lines, applications for line extensions and construction, and the merger with or acquisition of control of rail common carriers. The outcome of STB proceedings can affect the profitability of BNSF s business.

The DOT and OSHA have jurisdiction under several federal statutes over a number of safety and health aspects of rail operations, including the transportation of hazardous materials. State agencies regulate some aspects of rail operations with respect to health and safety in areas not otherwise preempted by federal law. BNSF Railway is required to transport these commodities to the extent of its common carrier obligation.

Environmental Matters

BNSF s rail operations, as well as those of its competitors, are also subject to extensive federal, state and local environmental regulation covering discharges to water, air emissions, toxic substances and the generation, handling, storage, transportation and disposal of waste and hazardous materials. This regulation has the effect of increasing the cost and liabilities associated with rail operations. Environmental risks are also inherent in rail operations, which frequently involve transporting chemicals and other hazardous materials.

Many of BNSF s land holdings are and have been used for industrial or transportation-related purposes or leased to commercial or industrial companies whose activities may have resulted in discharges onto the property. As a result, BNSF is now subject to, and will from time to time continue to be subject to, environmental cleanup and enforcement actions. In particular, the federal Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), also known as the Superfund law, generally imposes joint and several liabilities for the cleanup and enforcement costs on current and former owners and operators of a site, without regard to fault or the legality of the original conduct. Accordingly, BNSF may be responsible under CERCLA and other federal and state statutes for all or part of the costs to clean up sites at which certain substances may have been released by BNSF, its current lessees, former owners or lessees of properties, or other third parties. BNSF may also be subject to claims by third parties for investigation, cleanup, restoration or other environmental costs under environmental statutes or common law with respect to properties they own that have been impacted by BNSF operations.

Competition

The business environment in which BNSF operates is highly competitive. Depending on the specific market, deregulated motor carriers and other railroads, as well as river barges, ships and pipelines in certain markets, may exert pressure on price and service levels. The presence of advanced, high service truck lines with expedited delivery, subsidized infrastructure and minimal empty mileage continues to affect the market for non-bulk, time-sensitive freight. The potential expansion of longer combination vehicles could further encroach upon markets traditionally served by railroads. In order to remain competitive, BNSF and other railroads continue to develop and implement operating efficiencies to improve productivity.

As railroads streamline, rationalize and otherwise enhance their franchises, competition among rail carriers intensifies. BNSF s primary rail competitor in the Western region of the United States is the Union Pacific Railroad Company. Other Class I railroads and numerous regional railroads and motor carriers also operate in parts of the same territories served by BNSF. Based on weekly reporting by the Association of American Railroads, BNSF s share of the western United States rail traffic in 2014 was approximately 48.3%.

Utilities and Energy Businesses

Berkshire currently owns an 89.9% voting common stock interest in Berkshire Hathaway Energy Company (or BHE), which was renamed from MidAmerican Energy Holdings Company in 2014. BHE is an international energy company with subsidiaries that generate, transmit, store, distribute and supply energy. BHE s businesses are managed as separate operating units. BHE s domestic regulated energy interests are currently comprised of four regulated utility companies serving approximately 4.6 million retail customers, two interstate natural gas pipeline companies with approximately 16,400 miles of pipeline and a design capacity of approximately 7.8 billion cubic feet of natural gas per day and ownership interests in electricity transmission businesses. BHE s Great Britain electricity distribution subsidiaries serve about 3.9 million electricity end-users and its electricity transmission-only business in Alberta, Canada (acquired in 2014) serves approximately 85% of Alberta, Canada s population. BHE s interests also include a diversified portfolio of independent power projects, the second-largest residential real estate brokerage firm in the United States, and the second-largest residential real estate brokerage franchise network in the United States. BHE employs approximately 20,900 people in connection with its various operations.

General Matters

PacifiCorp is a regulated electric utility company headquartered in Oregon, serving electric customers in portions of Utah, Oregon, Wyoming, Washington, Idaho and California. The combined service territory s diverse regional economy ranges from rural, agricultural and mining areas to urban, manufacturing and government service centers. No single segment of the economy dominates the service territory, which helps mitigate PacifiCorp s exposure to economic fluctuations. In addition to retail sales, PacifiCorp sells electricity on a wholesale basis.

MidAmerican Energy Company (MEC) is a regulated electric and natural gas utility company headquartered in Iowa, serving electric and natural gas customers primarily in Iowa and also in portions of Illinois, South Dakota and Nebraska. MEC has a diverse customer base consisting of urban and rural residential customers and a variety of commercial and industrial customers. In addition to retail sales and natural gas transportation, MEC sells electricity principally to markets operated by regional transmission organizations and regulated natural gas on a wholesale basis and sells electricity and natural gas services in deregulated markets.

NV Energy, Inc. (NV Energy), acquired by BHE on December 19, 2013, is an energy holding company headquartered in Nevada, primarily consisting of two regulated utility subsidiaries, Nevada Power Company (Nevada Power) and Sierra Pacific Power Company (Sierra Pacific) (collectively, the Nevada Utilities). Nevada Power serves electric customers in southern Nevada and Sierra Pacific serves electric and natural gas customers in northern Nevada. The Nevada Utilities combined service territory s economy includes gaming, mining, recreation, warehousing, manufacturing and governmental services. In addition to retail sales and natural gas transportation, the Nevada Utilities sell electricity and natural gas on a wholesale basis.

As vertically integrated utilities, BHE s domestic utilities own approximately 26,000 net megawatts of generation capacity in operation and under construction. There are seasonal variations in these businesses that are principally related to the use of electricity for air conditioning and natural gas for heating. Typically, regulated electric revenues are higher in the summer months, while regulated natural gas revenues are higher in the winter months.

The Great Britain utilities consist of Northern Powergrid (Northeast) Limited and Northern Powergrid (Yorkshire) plc, which own a substantial electricity distribution network that delivers electricity to end-users in northeast England in an area covering approximately 10,000 square miles. The distribution companies primarily charge supply companies regulated tariffs for the use of its electrical infrastructure.

The natural gas pipelines consist of Northern Natural Gas Company (Northern Natural) and Kern River Gas Transmission Company (Kern River). Northern Natural is based in Nebraska and owns the largest interstate natural gas pipeline system in the United States, as measured by pipeline miles, reaching from southern Texas to Michigan s Upper Peninsula. Northern Natural s pipeline system consists of approximately 14,700 miles of natural gas pipelines. Northern Natural s extensive pipeline system, which is interconnected with many interstate and intrastate pipelines in the national grid system, has access to supplies from multiple major supply basins and provides transportation services to utilities and numerous other customers. Northern Natural also operates three underground natural gas storage facilities and two liquefied natural gas storage peaking units. Northern Natural s pipeline system experiences significant seasonal swings in demand and revenue, with the highest demand typically occurring during the months of November through March.

Kern River is based in Utah and owns an interstate natural gas pipeline system that consists of approximately 1,700 miles and extends from supply areas in the Rocky Mountains to consuming markets in Utah, Nevada and California. Kern River transports natural gas for electric utilities and natural gas distribution utilities, major oil and natural gas companies or affiliates of such companies, electricity generating companies, energy marketing and trading companies, and financial institutions.

AltaLink L.P. (AltaLink), acquired by BHE on December 1, 2014, is a regulated electric transmission-only utility company headquartered in Calgary, Alberta that serves approximately 85% of Alberta s population. AltaLink connects generation plants to major load centers, cities and large industrial plants throughout its 132,000 square mile service territory. AltaLink receives all of its regulated transmission tariffs from the Alberta Electric System Operator (AESO) based on tariffs approved by the Alberta Utilities Commission (AUC).

BHE Renewables is based in Iowa and owns interests in independent power projects that are in service or under construction in California, Illinois, Arizona, Texas, the Philippines, New York and Hawaii. These independent power projects primarily sell power generated from solar, wind, hydro and geothermal sources under long-term contracts.

Regulatory Matters

PacifiCorp, MEC and the Nevada Utilities are subject to comprehensive regulation by various federal, state and local agencies. The Federal Energy Regulatory Commission (FERC) is an independent agency with broad authority to implement provisions of the Federal Power Act, the Natural Gas Act (NGA), the Energy Policy Act of 2005 and other federal statutes. The FERC regulates rates for wholesale sales of electricity; transmission of electricity, including pricing and regional planning for the expansion of transmission systems; electric system reliability; utility holding companies; accounting and records retention; securities issuances; construction and operation of hydroelectric facilities; and other matters. The FERC also has the enforcement authority to assess civil penalties of up to $1 million per day per violation of rules, regulations and orders issued under the Federal Power Act. MEC is also subject to regulation by the Nuclear Regulatory Commission pursuant to the Atomic Energy Act of 1954, as amended, with respect to its ownership of the Quad Cities Nuclear Station.

With certain limited exceptions, BHE s domestic utilities have an exclusive right to serve retail customers within their service territories and, in turn, have an obligation to provide service to those customers. In some jurisdictions, certain classes of customers may choose to purchase all or a portion of their energy from alternative energy suppliers, and in some jurisdictions retail customers can generate all or a portion of their own energy. Historically, state regulatory commissions have established retail electric and natural gas rates on a cost-of-service basis, which are designed to allow a utility an opportunity to recover what each state regulatory commission deems to be the utility s reasonable costs of providing services, including a fair opportunity to earn a reasonable return on its investments based on its cost of debt and equity. The retail electric rates of PacifiCorp, MEC and the Nevada Utilities are generally based on the cost of providing traditional bundled services, including generation, transmission and distribution services.

Northern Powergrid (Northeast) and Northern Powergrid (Yorkshire) each charge fees for the use of their distribution systems that are controlled by a formula prescribed by the British electricity regulatory body, the Gas and Electricity Markets Authority. The current five-year price control period is scheduled to end March 31, 2015, and the next price control period is set for the eight-year period ending March 31, 2023.

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The natural gas pipelines are subject to regulation by various federal, state and local agencies. The natural gas pipeline and storage operations of Northern Natural and Kern River are regulated by the FERC pursuant to the NGA and the Natural Gas Policy Act of 1978. Under this authority, the FERC regulates, among other items, (a) rates, charges, terms and conditions of service and (b) the construction and operation of interstate pipelines, storage and related facilities, including the extension, expansion or abandonment of such facilities. Interstate natural gas pipeline companies are also subject to regulations administrated by the Office of Pipeline Safety within the Pipeline and Hazardous Materials Safety Administration, an agency within the DOT. Federal pipeline safety regulations are issued pursuant to the Natural Gas Pipeline Safety Act of 1968, as amended, which establishes safety requirements in the design, construction, operation and maintenance of interstate natural gas pipeline facilities.

AltaLink is regulated by the AUC, pursuant to the Electric Utilities Act (Alberta), the Public Utilities Act (Alberta), the Alberta Utilities Commission Act (Alberta) and the Hydro and Electric Energy Act (Alberta). The AUC is an independent quasi-judicial agency with broad authority to impact AltaLink s General Tariff Applications, rates, construction, operations and financing. Under the Electric Utilities Act, AltaLink prepares and files applications with the AUC for approval of tariffs to be paid by the AESO for the use of its transmission facilities, and the terms and conditions governing the use of those facilities. The AESO is the independent system operator in Alberta, Canada that oversees Alberta s integrated electrical system (AIES) and wholesale electricity market. The AESO is responsible for directing the safe, reliable and economic operation of the AIES for the use of transmission facilities and the terms and conditions governing the use of those facilities.

Environmental Matters

BHE and its energy businesses are subject to federal, state, local and foreign laws and regulations regarding air and water quality, renewable portfolio standards, emissions performance standards, climate change, coal combustion byproduct disposal, hazardous and solid waste disposal, protected species and other environmental matters that have the potential to impact current and future operations. In addition to imposing continuing compliance obligations, these laws and regulations, such as the Federal Clean Air Act, provide regulators with the authority to levy substantial penalties for noncompliance including fines, injunctive relief and other sanctions.

The Federal Clean Air Act, as well as state laws and regulations impacting air emissions, provides a framework for protecting and improving the nation s air quality and controlling sources of air emissions. These laws and regulations continue to be promulgated and implemented and will impact the operation of BHE s generating facilities and require them to reduce emissions at those facilities to comply with the requirements.

Renewable portfolio standards have been established by certain state governments and generally require electricity providers to obtain a minimum percentage of their power from renewable energy resources by a certain date. Utah, Oregon, Washington, California, Iowa and Nevada have adopted renewable portfolio standards. In addition, the potential adoption of state or federal clean energy standards, which include low-carbon, non-carbon and renewable electricity generating resources, may also impact electricity generators and natural gas providers.

Comprehensive climate change legislation has not been adopted by Congress; however, regulation of greenhouse gas emissions under various provisions of the Federal Clean Air Act has continued since the Environmental Protection Agency s December 2009 findings that greenhouse gas emissions threaten public health and welfare. Since that determination, significant sources of greenhouse gas emissions have been required to report their greenhouse gas emissions and to undergo a best available control technology determination in conjunction with permitting greenhouse gas emissions. As part of President Obama s Climate Action Plan issued in June 2013, the Environmental Protection Agency was required to re-propose by September 2013 greenhouse gas new source performance standards that had originally been proposed in 2012 for new fossil-fueled power plants. The re-proposed standards for new sources were released in September 2013 and generally propose a standard of 1,000 pounds of carbon dioxide per megawatt hour for natural gas-fueled combustion turbines and 1,100 pounds of carbon dioxide per megawatt hour for coal-fueled units. In addition, the Climate Action Plan required the Environmental Protection Agency to issue proposed standards or guidelines to address greenhouse gas emissions from existing fossil-fueled electric generating units by June 2014, to finalize those standards or guidelines by June 2015, and to require states to submit implementation plans by June 2016. The proposed guidelines were released by the Environmental Protection Agency in June 2014, and set state-by-state emission targets for carbon dioxide based on the application of the Best System of Emission Reduction, consisting of four building blocks: (1) a 6% heat rate improvement at coal-fueled units; (2) re-dispatch of natural gas combined cycle units up to a 70% capacity factor; (3) increased deployment of renewable and non-carbon generation; and, (4) increased deployment of end use energy efficiency. With a 2020 effective date, the proposed guidelines would achieve a reduction in carbon dioxide emissions from existing fossil-fueled electric generating units of 30% below 2005 levels by 2030. The public comment period closed December 1, 2014, and the Environmental Protection Agency is expected to issue its final guidelines to address carbon dioxide emissions from existing fossil-fueled electric generating units in the summer of 2015 at the same time the agency releases the final new source performance standards for modified and new sources.

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In November 2014, President Obama announced a climate agreement with China in which the U.S. agreed to reduce greenhouse gas emissions 26-28% by 2025 from 2005 levels and China agreed that its emissions would peak by 2030 and it would aim to have 20% of its energy sources be non-carbon. While the discussions continue at the federal and international level over the direction of climate change policy, several states have continued to implement state-specific laws or regional initiatives to mitigate greenhouse gas emissions.

The impact of future federal, regional, state and international accords, legislation, regulation or judicial proceedings related to climate change cannot be quantified in any meaningful range at this time. New requirements limiting greenhouse gas emissions could have a material adverse impact on BHE and its subsidiaries, depending on the timing and scope of such requirements.

BHE continues to take actions to mitigate greenhouse gas emissions. For example, as of December 31, 2014, BHE subsidiaries owned 5,168 megawatts of wind-powered generating capacity in operation and under construction, which when completed is estimated to cost over $9 billion, and 1,286 megawatts of solar generating capacity in operation and under construction, which when completed is estimated to cost approximately $6 billion.

Non-Energy Businesses

BHE also owns HomeServices of America, Inc. (HomeServices), the second largest full-service residential real estate brokerage firm in the United States. In addition to providing traditional residential real estate brokerage services, HomeServices offers other integrated real estate services, including mortgage originations and mortgage banking, title and closing services, property and casualty insurance, home warranties, relocation services and other home-related services. It operates under 30 residential real estate brand names with over 24,000 sales associates in over 460 brokerage offices in 25 states.

HomeServices principal sources of revenue are dependent on residential real estate sales, which are generally higher in the second and third quarters of each year. This business is highly competitive and subject to the general real estate market conditions.

In October 2012, HomeServices acquired a 66.7% interest in the second largest residential real estate brokerage franchise network in the United States, which offers and sells independently owned and operated residential real estate brokerage franchises. HomeServices franchise network currently includes over 440 franchisees in over 1,500 brokerage offices in 49 states with over 43,000 sales associates under three brand names. In exchange for certain fees, HomeServices provides the right to use the Berkshire Hathaway HomeServices, Prudential and Real Living brand names and other related service marks. In 2013, HomeServices began rebranding certain of its Prudential franchisees as Berkshire Hathaway HomeServices. As of December 31, 2014, over 170 franchisees have been rebranded.

McLane Company McLane Company, Inc. (McLane) provides wholesale distribution services in all 50 states to customers that include convenience stores, discount retailers, wholesale clubs, drug stores, military bases, quick service restaurants and casual dining restaurants. McLane provides wholesale distribution services to Wal-Mart Stores, Inc. (Wal-Mart), which accounts for approximately 24% of McLane s revenues. McLane also has other significant customers, including 7-Eleven and Yum! Brands. A curtailment of purchasing by Wal-Mart or its other significant customers could have a material adverse impact on McLane s periodic revenues and earnings. McLane s business model is based on a high volume of sales, rapid inventory turnover and stringent expense controls. Operations are currently divided into four business units: grocery distribution, foodservice distribution, beverage distribution, and software development. In 2014, the grocery and foodservice units comprised approximately 98.5% of the total revenues of the company. McLane and its subsidiaries employ approximately 22,000 associates.

McLane s grocery distribution unit, based in Temple, Texas, maintains a dominant market share within the convenience store industry and serves most of the national convenience store chains and major oil company retail outlets. Grocery operations provide products to approximately 46,000 retail locations nationwide, including Wal-Mart. McLane s grocery distribution unit operates 23 facilities in 19 states.

McLane s foodservice distribution unit, based in Carrollton, Texas, focuses on serving the quick service restaurant industry with high quality, timely-delivered products. Operations are conducted through 18 facilities in 16 states. The foodservice distribution unit services approximately 21,000 chain restaurants nationwide. On August 24, 2012, McLane acquired Meadowbrook Meat Company (MBM). MBM, based in Rocky Mount, North Carolina, is a large customized foodservice distributor for national restaurant chains. MBM operates from 34 distribution facilities in 16 states. MBM services approximately 15,000 chain restaurants nationwide.

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On April 23, 2010, McLane acquired Kahn Ventures, parent company of Empire Distributors and Empire Distributors of North Carolina. Kahn Ventures and its subsidiaries are wholesale distributors of distilled spirits, wine and beer. Operations are conducted through nine distribution centers in two states. Kahn Ventures acquired Horizon Wine and Spirits, Inc., on December 31, 2010, Delta Wholesale Liquors on April 30, 2012 and Baroness Small Estates, Inc., a wine distributor, on February 21, 2014. These operations are conducted through three distribution centers located in Tennessee and in Colorado. The beverage unit services approximately 19,000 retail locations in the Southeastern United States and Colorado.

Manufacturing Businesses

Berkshire s numerous and diverse manufacturing businesses are grouped into three categories: (1) industrial and end-user products, (2) building products and (3) apparel. Each of these business groups are described below.

Industrial and end-user products

In 2008, Berkshire acquired approximately 64% of the outstanding common stock of Marmon Holdings, Inc. (Marmon), a private company then owned by trusts for the benefit of members of the Pritzker Family of Chicago. On various dates in 2010, 2012 and 2013, Berkshire acquired additional shares of outstanding stock held by noncontrolling shareholders and beginning as of December 31, 2013 owned substantially all of Marmon. Marmon is currently comprised of three autonomous companies consisting of thirteen diverse business sectors and approximately 185 independent manufacturing and service businesses. Marmon operates approximately 358 manufacturing, distribution and service facilities, which are located primarily in the United States, as well as in 22 other countries worldwide. Marmon s transportation equipment manufacturing, repair and leasing businesses under UTLX Company are discussed in Finance and Financial Products businesses. Marmon s other diversified manufacturing and service operations are referred to as Marmon manufacturing and discussed further below.

Marmon manufacturing includes Marmon Engineered Components Company (Engineered Components), Marmon Retail Technologies Company (Retail Technologies) and the Engineered Wire & Cable operations within Marmon Energy Services Company (Energy Services). The *Engineered Wire & Cable* sector supplies electrical and electronic wire and cable for energy related markets and other industries.

Marmon Engineered Components includes the following three sectors: *Distribution Services* provides specialty metal pipe and tubing, bar and sheet products to markets including construction, industrial, aerospace and many others; *Electrical & Plumbing Distribution Products* supplies electrical building wire primarily for residential and commercial construction, and copper tube for the plumbing, HVAC, refrigeration and industrial markets, through the wholesale channel; and *Industrial Products* manufactures and markets metal fasteners and fastener coatings for the construction, industrial and other markets, gloves for industrial markets, portable lighting equipment for mining and safety markets and overhead electrification equipment for mass transit systems. *Industrial Products* also provides custom-machined aluminum and brass forgings for the construction, energy, recreation and other industries, brass fittings and valves for commercial and industrial applications, and drawn aluminum tubing and extruded aluminum shapes for the construction, automotive, appliance, medical and other markets.

Marmon Retail Technologies includes the following seven sectors: *Foodservice Technologies* supplies commercial food preparation equipment for restaurants and fast food chains; *Beverage Technologies* produces beverage dispensing and cooling equipment to foodservice retailers; *Highway Technologies* primarily serves the heavy-duty highway transportation industry with trailers, fifth wheel coupling devices and undercarriage products such as brake parts and suspension systems, and also serves the light vehicle aftermarket with clutches and related products; *Retail Store Equipment* provides shelving systems, other merchandising displays and related services and shopping carts for retail stores as well as material handling and security carts and automation equipment for many industries; *Retail Science* delivers retail market solutions to brands and retailers including merchandising displays, in-store digital merchandising and marketing programs; *Water Treatment* manufactures and markets residential water softening, purification and refrigeration filtration systems, treatment systems for industrial markets including power generation, oil and gas, chemical, and pulp and paper, gear drives for irrigation systems and cooling towers, and air-cooled heat exchangers; and *Retail Products* supplies electrical building wire, plumbing tube and brass fittings through the home center channel as well as work and garden gloves sold at retail.

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In September 2011, Berkshire acquired The Lubrizol Corporation (Lubrizol). Lubrizol is a specialty chemical company that produces and supplies technologies for the global transportation, industrial, oilfield and consumer markets. Since 2011, Lubrizol has completed a number of bolt-on acquisitions, including three in 2014. On August 1, 2014, Lubrizol completed the acquisition of Vesta, a leading contract manufacturer of silicone medical products and thermoplastic extruded components for the medical device industry. On December 31, 2014, Lubrizol, acquired Warwick Chemicals, a leading global developer, producer and supplier of stain removal technology with hygiene benefits for fabric care applications. On December 31, 2014, Lubrizol also completed the acquisition in the United States and Canada of Weatherford International s global oilfield chemicals business, known as Engineered Chemistry and its United States drilling fluids business, known as Integrity Industries. Lubrizol also agreed to acqui