charged with $1,474,000 and $1,330,000 in providing for the benefits accrued during 1978 and 1977, respectively.

The Company has an incentive plan for key employees that provides for an incentive fund based upon the attainment of a specific return on investment and income before taxes and interest. Operating expense has been charged with $2,300,000 and $2,156,000 during the years 1978 and 1977, respectively, in providing for the benefits accrued.

### 8. Income Taxes

Income tax expense has the following components:

| | Years Ending December 31, 1978 | 1977 (Restated) |
|---|---|---|
| Federal: | | |
| Current | $28,603,000 | $31,627,000 |
| Deferred | 12,400,000 | 5,453,000 |
| | 41,003,000 | 37,080,000 |
| State | 5,801,000 | 5,696,000 |
| Foreign: | | |
| Current | 4,649,000 | 3,420,000 |
| Deferred | 1,240,000 | 822,000 |
| | 5,889,000 | 4,242,000 |
| Total | $52,693,000 | $47,018,000 |

Deferred taxes for the years ended December 31, 1978 and 1977 result from the differences shown in Table 2, below.

The differences between the statutory and effective income tax rates for the years ended December 31, 1978 and 1977 are shown in Table 3, below.

The provisions for income taxes for the years 1978 and 1977 have been reduced by $6,791,000 and $5,506,000, respectively, for investment tax credit.

At December 31, 1978 and 1977, consolidated earnings retained in the business included approximately $16,200,000 and $15,300,000, respectively, on which Federal income tax has not been provided since the Company has reinvested such earnings and intends to continue such investment permanently in export activities and foreign corporations.

### 9. Acquisitions

The financial statements for 1978 include two acquisitions accounted for as purchases: Sully-Miller Contracting Company, acquired for approximately $34,700,000, and Tennessee Land and Mining Company, acquired for approximately $21,859,000. The financial statements include four acquisitions made in 1977 using the purchase method of accounting. The most significant of these is Kaiser Sand and Gravel Company, a division of Kaiser Industries, which was acquired for $20,100,000. Results of operations of these acquisitions have been included from their respective acquisition dates. The following summary, prepared on a pro forma basis, combines the consolidated results of operations of the Company for the years ended December 31, 1978 and 1977 with the pre-acquisition earnings of these acquisitions:

| | 1978 | 1977 |
|---|---|---|
| Net sales | $1,651,504,000 | $1,566,892,000 |
| Net income | $ 75,871,000 | $ 70,641,000 |
| Earnings per share of common stock | $3.01 | $2.81 |

The Company has completed an Agreement of Merger providing for the acquisition of Ivy Corporation. As provided in the Agreement each outstanding share of Ivy common stock has been converted into 0.6 share of Koppers common stock (a total of 952,723 Koppers Company, Inc. shares).

### 10. Foreign Operations

The Company's Consolidated Balance Sheet and Consolidated Statement of Income include the following amounts relating to consolidated subsidiaries (all wholly owned) located outside the United States:

| | 1978 | 1977 |
|---|---|---|
| Assets | $67,973,000 | $ 86,303,000 |
| Liabilities | $30,984,000 | $ 44,521,000 |
| Sales | $99,756,000 | $116,242,000 |
| Net income | $ 5,701,000 | $ 5,024,000 |

### 11. Operations by Industry Segment

The Company operates principally in five industry segments. Information relating to the products and services provided by these segments is located on pages 12 through 25 of this annual report and 10-K. Intersegment sales are not disclosed in Table 4, right, because of immateriality.

### 12. Quarterly Financial Data (Unaudited)

The effect of the change in accounting for leases (see Note 5) has been included in the fourth quarter for 1978 and 1977 since the effect was not material. Gross profit has been increased by $1,841,000 and net income increased by $211,000 (1¢ per common share) in 1977 as a result of the accounting change.

During the fourth quarter of 1978, net income increased by $8,859,000 (34¢ per share) as a result of the profit recognized on the sale of the Cutler-Hammer, Inc. investment.

**Table 2. Deferred Taxes**

| | 1978 | 1977 (Restated) |
|---|---|---|
| Difference in book and tax income recognition methods on sale of investment in Cutler-Hammer, Inc. | $ 8,706,000 | $ — |
| Reversal of prior provision upon sale of foreign subsidiary | (552,000) | — |
| Excess of tax over book depreciation | 5,828,000 | 7,080,000 |
| Reversal of prior provisions related to inventory costing adjustments | (450,000) | (450,000) |
| Difference in book and tax income recognition methods on contracts of foreign subsidiary | 491,000 | (772,000) |
| Other—net | (383,000) | 417,000 |
| | $13,640,000 | $6,275,000 |

**Table 3. Statutory and Effective Income Tax Rates**

| | 1978 | 1977 (Restated) |
|---|---|---|
| Statutory tax rate: | | |
| Federal | 48.0% | 48.0% |
| State, net of Federal tax benefit | 2.3% | 2.6% |
| Investment tax credit | (5.0%) | (4.5%) |
| Nontaxable earnings of Domestic International Sales Corporation | (.5%) | (1.3%) |
| Effect of percentage over cost depletion | (1.7%) | (1.1%) |
| Effect of lower statutory tax rate applicable to capital gain income | (.4%) | (.5%) |
| Other—net | (1.8%) | (1.7%) |
| | 40.9% | 41.5% |