

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q

☒ Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended May 31, 1998 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 0-22496

SCHNITZER STEEL INDUSTRIES, INC.

-----  
(Exact name of registrant as specified in its charter)

OREGON

93-0341923

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(I.R.S. Employer  
Identification No.)

3200 N.W. Yeon Ave., P.O Box 10047  
Portland, OR

97296-0047

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(503) 224-9900

-----  
(Registrant's telephone number, including area code)

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 ☒ No ☐

The Registrant had 5,555,026 shares of Class A Common Stock, par value of \$1.00 per share and 4,430,328 shares of Class B Common Stock, par value of \$1.00 per share outstanding at July 1, 1998.

SCHNITZER STEEL INDUSTRIES, INC.

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SCHNITZER STEEL INDUSTRIES, INC.  
CONSOLIDATED BALANCE SHEET  
(in thousands, except per share amounts)

	May 31, 1998	August 31, 1997
	----- (Unaudited)	----- (Audited)
ASSETS		
CURRENT ASSETS:		
Cash	\$ 1,666	\$ 3,106
Accounts receivable, less allowance for doubtful accounts of \$485 and \$524	30,043	31,010
Accounts receivable from related parties	499	1,215
Inventories (Note 2)	104,506	95,154
Deferred income taxes	10,737	10,737
Prepaid expenses and other	6,834	3,168
	-----	-----
TOTAL CURRENT ASSETS	154,285	144,390
	-----	-----
NET PROPERTY, PLANT AND EQUIPMENT	142,925	151,136
	-----	-----
OTHER ASSETS:		
Investment in joint venture partnerships	105,578	74,605
Advances to joint venture partnerships	9,161	7,145
Goodwill	41,320	42,230
Intangibles and other	9,753	8,480
	-----	-----
	\$ 463,022	\$ 427,986
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Current portion of long-term debt (Note 7)	\$ 166	\$ 361
Accounts payable	15,673	19,456
Accrued payroll liabilities	4,355	5,158
Current portion of environmental liabilities (Note 4)	5,152	5,787
Other accrued liabilities	9,107	8,730
	-----	-----
TOTAL CURRENT LIABILITIES	34,453	39,492
	-----	-----
DEFERRED INCOME TAXES	28,117	28,409
	-----	-----
LONG-TERM DEBT LESS CURRENT PORTION (Note 7)	128,988	92,881
	-----	-----
ENVIRONMENTAL LIABILITIES, NET OF CURRENT PORTION (Note 4)	23,030	24,530
	-----	-----
OTHER LONG-TERM LIABILITIES	3,311	3,613
	-----	-----
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY:		
Preferred stock--20,000 shares authorized, none issued		
Class A common stock--75,000 shares \$1 par value authorized, 5,555 and 5,737 shares issued and outstanding	5,555	5,737
Class B common stock--25,000 shares \$1 par value authorized, 4,431 and 4,445 shares issued and outstanding	4,431	4,445
Additional paid-in capital	105,124	109,994
Retained earnings	130,013	118,885
	-----	-----
	245,123	239,061
	-----	-----
	\$ 463,022	\$ 427,986
	=====	=====

The accompanying notes are an integral part of this statement.

SCHNITZER STEEL INDUSTRIES, INC.  
CONSOLIDATED STATEMENT OF OPERATIONS  
(in thousands, except per share amounts)

(unaudited)

	For The Three Months Ended May 31,		For The Nine Months Ended May 31,	
	1998	1997	1998	1997
REVENUES	\$ 80,918	\$ 89,297	\$ 268,216	\$ 248,596
COSTS AND EXPENSES:				
Cost of goods sold and other operating expenses	71,296	76,230	237,567	219,434
Selling and administrative	5,520	4,888	16,150	15,443
	76,816	81,118	253,717	234,877
INCOME FROM JOINT VENTURES	1,417	2,720	8,380	4,500
INCOME FROM OPERATIONS	5,519	10,899	22,879	18,219
OTHER INCOME (EXPENSE):				
Interest expense	(1,849)	(1,551)	(4,537)	(3,583)
Other income	283	3,416	1,096	4,441
	(1,566)	1,865	(3,441)	858
INCOME BEFORE INCOME TAXES	3,953	12,764	19,438	19,077
Income tax provision	(1,384)	(4,340)	(6,803)	(6,494)
NET INCOME	\$ 2,569	\$ 8,424	\$ 12,635	\$ 12,583
BASIC EARNINGS PER SHARE	\$ 0.26	\$ 0.81	\$ 1.25	\$ 1.22
DILUTED EARNINGS PER SHARE	\$ 0.26	\$ 0.81	\$ 1.25	\$ 1.21

The accompanying notes are an integral part of this statement.

SCHNITZER STEEL INDUSTRIES, INC.  
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY  
(in thousands)

(unaudited)

	Class A Common Stock		Class B Common Stock		Additional Paid-in Capital	Retained Earnings	Total
	Shares	Amount	Shares	Amount			
BALANCE AT 8/31/96	5,773	\$ 5,773	4,575	\$ 4,575	\$ 113,747	\$ 99,718	\$ 223,813
Class B common stock converted to Class A common stock	130	130	(130)	(130)			
Class A common stock repurchased	(166)	(166)			(3,753)		(3,919)
Net income						21,225	21,225
Dividends paid						(2,058)	(2,058)
	-----	-----	-----	-----	-----	-----	-----
BALANCE AT 8/31/97	5,737	5,737	4,445	4,445	109,994	118,885	239,061
Net Income						12,635	12,635
Class B common stock converted to Class A common stock	14	14	(14)	(14)			
Class A common stock repurchased	(196)	(196)			(4,870)		(5,066)
Dividends paid						(1,507)	(1,507)
	-----	-----	-----	-----	-----	-----	-----
BALANCE AT 5/31/98	5,555	\$ 5,555	4,431	\$ 4,431	\$ 105,124	\$ 130,013	\$ 245,123
	=====	=====	=====	=====	=====	=====	=====

The accompanying notes are an integral part of this statement.

SCHNITZER STEEL INDUSTRIES, INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS  
(in thousands)

(unaudited)

	For The Nine Months Ended May 31,	
	1998	1997
<b>OPERATIONS:</b>		
Net income	\$ 12,635	\$ 12,583
Noncash items included in income:		
Depreciation and amortization	14,123	13,055
Deferred income taxes	(292)	(2,211)
Equity in earnings of joint ventures and other investments	(8,380)	(4,500)
Gain on disposal of assets	(113)	(65)
Cash provided (used) by assets and liabilities:		
Accounts receivable	1,683	64
Inventories	(9,352)	(13,618)
Prepaid expenses and other	(2,608)	1,855
Accounts payable	(3,783)	(5,987)
Deferred revenue	(76)	3,327
Accrued expenses	(351)	1,855
Environmental liabilities	(2,135)	(861)
Other assets and liabilities	(1,491)	(367)
NET CASH (USED) PROVIDED BY OPERATIONS	(140)	5,130
<b>INVESTMENTS:</b>		
Payment for purchase of Proler		(42,456)
Capital expenditures	(7,512)	(10,499)
Advances to joint ventures	(2,016)	(4,396)
Investments in joint ventures	(22,892)	18,721
Proceeds from sale of assets	2,986	4,859
Other	(1,205)	(1,057)
NET CASH USED BY INVESTMENTS	(30,639)	(34,828)
<b>FINANCING:</b>		
Repurchase of Class A common stock	(5,066)	(2,350)
Dividends declared and paid	(1,507)	(1,551)
Increase in long-term debt	36,200	63,526
Reduction in long-term debt	(288)	(27,866)
NET CASH PROVIDED BY FINANCING	29,339	31,759
NET (DECREASE) INCREASE IN CASH	(1,440)	2,061
CASH AT BEGINNING OF PERIOD	3,106	1,896
CASH AT END OF PERIOD	\$ 1,666	\$ 3,957

The accompanying notes are an integral part of this statement.

SCHNITZER STEEL INDUSTRIES, INC.  
NOTES TO FINANCIAL STATEMENTS  
FOR THE NINE MONTHS ENDED MAY 31, 1998 and 1997  
(in thousands, except per share amounts)  
(Unaudited)

Note 1 - Summary Of Significant Accounting Policies:

Basis of Presentation  
-----

The accompanying unaudited interim financial statements of Schnitzer Steel Industries, Inc. (the Company) have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and note disclosures normally included in annual financial statements have been condensed or omitted pursuant to those rules and regulations. In the opinion of management, all adjustments, consisting only of normal, recurring adjustments considered necessary for a fair presentation, have been included. Although management believes that the disclosures made are adequate to ensure that the information presented is not misleading, it is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the Company's annual report for the fiscal year ended August 31, 1997. The results for the nine months ended May 31, 1998 are not necessarily indicative of the results of operations for the entire year.

Earnings Per Share  
-----

The Company has adopted Statement of Financial Accounting Standards ("SFAS") No. 128 "Earnings Per share", which specifies the computation, presentation and disclosure requirements for earnings per share ("EPS"). SFAS 128 replaces the presentation of primary and fully diluted EPS with basic and diluted EPS. Basic EPS is computed based upon the weighted average number of common shares outstanding during the period. Diluted EPS reflects the potential dilution that would occur if securities or other contracts to issue common stock were exercised or converted into common stock. The following represents a reconciliation from basic EPS to diluted EPS:

Three Months Ended May 31, 1998			
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Basic EPS	\$ 2,569	9,985	\$ 0.26
Options	--	62	=====
Diluted EPS	\$ 2,569	10,047	\$ 0.26
	=====	=====	=====

Three Months Ended May 31, 1997			
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Basic EPS	\$ 8,424	10,343	\$ 0.81
Options	--	28	=====
Diluted EPS	\$ 8,424	10,371	\$ 0.81
	=====	=====	=====

SCHNITZER STEEL INDUSTRIES, INC.  
NOTES TO FINANCIAL STATEMENTS  
FOR THE NINE MONTHS ENDED MAY 31, 1998 and 1997  
(in thousands, except per share amounts)  
(Unaudited)

Nine Months Ended May 31, 1998			
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Basic EPS	\$ 12,635	10,070	\$ 1.25
Options	--	71	=====
Diluted EPS	\$ 12,635	10,141	\$ 1.25
	=====	=====	=====

Nine Months Ended May 31, 1997			
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Basic EPS	\$ 12,583	10,340	\$ 1.22
Options	--	59	=====
Diluted EPS	\$ 12,583	10,399	\$ 1.21
	=====	=====	=====

Note 2 - Inventories:

Inventories consist of the following (in thousands):

	May 31, 1998	August 31, 1997
	(Unaudited)	(Audited)
Scrap metals	\$ 25,864	\$ 26,897
Work in process	11,783	24,358
Finished goods	50,690	28,109
Supplies	16,169	15,790
	-----	-----
	\$ 104,506	\$ 95,154
	=====	=====

Scrap metal inventories are valued at LIFO; the remainder are at FIFO. Interim LIFO calculations are based on the Company's estimates of expected year-end inventory levels and costs. The cost of scrap metal inventories exceeded the stated LIFO value by \$8,039 at May 31, 1998 and August 31, 1997.

SCHNITZER STEEL INDUSTRIES, INC.  
NOTES TO FINANCIAL STATEMENTS  
FOR THE NINE MONTHS ENDED MAY 31, 1998 and 1997  
(in thousands, except per share amounts)  
(Unaudited)

Note 3 - Related Party Transactions:

Certain shareholders of the Company own significant interests in, or are related to owners of, the entities discussed below. As such, these entities are considered related parties for financial reporting purposes.

Transactions Affecting Cost of Goods Sold and Other Operating Expenses  
-----

The Company charters several vessels from related shipping companies to transport scrap metal to foreign markets. In 1993, the Company signed a five-year time-charter agreement for one vessel. The agreement guarantees the ship owner a residual market value of \$2,500 at the end of the time-charter. The Company entered into two additional seven-year time-charters in May 1995. Charges incurred for these charters were \$1,522 and \$1,841 for the three months ended May 31, 1998 and 1997, respectively, and \$5,836 and \$6,332 for the nine months ended May 31, 1998 and 1997, respectively.

The Company purchased scrap metals from certain of its joint venture operations totaling \$4,452 and \$3,879 for the three months ended May 31, 1998 and 1997, respectively, and \$12,307 and \$9,019 for the nine months ended May 31, 1998 and 1997, respectively.

The Company leases certain land and buildings from a real estate company which is a related entity. The rent expense was \$338 and \$387 for the three months ended May 31, 1998 and 1997, respectively, and \$998 and \$1,098 for the nine months ended May 31, 1998 and 1997, respectively.

Transactions Affecting Selling and Administrative Expenses  
-----

The Company performs some administrative services and provides operation and maintenance of management information systems for certain related parties. These services are charged to the related parties based upon costs plus a 15% margin for overhead and profit. The administrative charges totaled \$233 and \$285 for the three months ended May 31, 1998 and 1997, respectively, and \$969 and \$795 for the nine months ended May 31, 1998 and 1997, respectively.

Transactions Affecting Other Income (Expense)  
-----

The vessels discussed above are periodically sub-chartered to third parties. In this case, a related shipping agency company acts as the Company's agent in the collection of income and payment of expenses related to sub-charter activities. Charges incurred for these sub-charters were \$123 for the three months ended May 31, 1998, and \$743 and \$871 for the nine months ended May 31, 1998 and 1997, respectively. There was no subcharter income for the three months ended May 31, 1998 and 1997. These charges were offset by income of \$408 and \$747 for the nine months ended May 31, 1998 and 1997, respectively.



SCHNITZER STEEL INDUSTRIES, INC.  
NOTES TO FINANCIAL STATEMENTS  
FOR THE NINE MONTHS ENDED MAY 31, 1998 and 1997  
(in thousands, except per share amounts)  
(Unaudited)

Note 4 - Environmental Liabilities:

During fiscal 1995, in conjunction with the due diligence proceedings for the Company's acquisition of Manufacturing Management, Inc. (MMI), the Company hired an independent third-party consultant to estimate the costs to cure both current and future potential environmental liabilities. The cumulative provision for the total cost specified in the consultant's report was included in MMI's statement of operations prior to its acquisition by the Company. This reserve was carried over to the Company's balance sheet and at May 31, 1998 aggregated \$20,200.

A portion of the liability recorded in fiscal 1995 relates to MMI's status as a potentially responsible party (PRP) for the investigation and cleanup of sediment along the Hylebos Waterway, on which the Schnitzer Steel of Tacoma (SST) scrap yard is located. SST and five other PRPs voluntarily entered into an Administrative Order of Consent with the Environmental Protection Agency (EPA) to fund a pre-remedial study of sediment contamination and remediation alternatives. SST's share of the study, which is expected to be complete in 1998, is approximately \$2,000. Any further potential liabilities, if any, cannot be estimated at this time.

In 1996, prior to the Company's acquisition of Proler International Corp. (Proler) (see Note 5), an independent third party consultant was engaged to estimate the costs to cure present and future potential liabilities related to Proler's wholly-owned and joint venture properties. Proler recorded a liability of \$8,600 for the probable costs to remediate its wholly-owned properties based upon the consultant's estimates, increasing its environmental reserves to \$9,800. The Company carried over the aggregate reserve to its financial statements upon acquiring Proler and \$8,000 remained outstanding on May 31, 1998. Concurrently, based upon the consultant's estimates, Proler's joint venture operations recorded additional liabilities of \$4,100 for the probable costs to remediate their properties. The liability was recorded prior to the Company's acquisition of Proler.

Between 1982 and 1987, MRI Corporation (MRI), a wholly-owned subsidiary of Proler, operated a tin can shredding and detinning facility in Tampa, Florida. In 1989 and 1992, the EPA conducted a preliminary site investigation of this property, and in December 1996, added the site to the "National Priorities List". MRI and Proler, along with several other parties, have been named as PRPs for this site by the EPA. Proler included the probable costs associated with this site in the aforementioned reserve. Additionally, Proler and this subsidiary have been named or identified as PRPs at several other sites.

As part of the Proler acquisition, the Company became a fifty-percent owner of Hugo Neu-Proler Company (HNP). HNP has agreed, as part of its lease renewal with the Port of Los Angeles, to be responsible for a multi-year, remedial clean-up project involving certain environmental conditions at its Terminal Island Site in Los Angeles, California by the year 2001. Remediation will include limited excavation and treatment of contaminated soils, paving, installation of a stormwater management system, construction of a noise barrier and perimeter wall around the facility and groundwater monitoring. The probable costs to remediate this property are included in the aforementioned reserve.

Certain of the Company's joint ventures have completed acquisitions or made investments in joint ventures. Prior to the closing of these transactions, the joint ventures caused environmental liabilities totaling approximately \$5.0 million to be recorded on the books of these new entities.

SCHNITZER STEEL INDUSTRIES, INC.  
NOTES TO FINANCIAL STATEMENTS  
FOR THE NINE MONTHS ENDED MAY 31, 1998 and 1997  
(in thousands, except per share amounts)  
(Unaudited)

Note 5 - Acquisition of Proler International Corp.:

Between November 29, 1996 and December 6, 1996, PIC Acquisition Corp. (PIC), a wholly-owned subsidiary of the Company, acquired 100% of the common stock of Proler. On December 6, 1996, the Company completed the merger of PIC with Proler and, as a result, Proler became a wholly-owned subsidiary of the Company.

The Company accounted for this acquisition using the purchase method. Accordingly, the purchase price has been allocated to the assets acquired and the liabilities assumed based on their estimated fair values as of the effective date of the acquisition.

The following unaudited pro forma information presents a summary of consolidated results of operations of the Company and Proler as though the acquisition had occurred at the beginning of the period shown.

	For the Nine Months Ended May 31, 1997
	-----
Revenues	\$ 251,742
Net income	\$ 5,964
	=====
Earnings per share	\$ .57
	=====

These pro forma results have been prepared for comparative purposes only and include certain adjustments to give effect for the acquisition, together with related income tax effects. They do not purport to be indicative of the results of operations which actually would have resulted had the combination been in effect at the beginning of the period presented or of future results of operations of the consolidated entities.

Note 6 - Disposal of Lathrop, California Facility:

In May 1998, the Company disposed of a tin scrap processing facility in Lathrop, California. The facility was acquired as part of the Proler acquisition (Note 5). The sale resulted in a gain of \$1.1 million, of which \$.8 million was recorded as a reduction in cost of goods sold and \$.3 million as a gain on sale of assets for the three months ended May 31, 1998.

Note 7 - Interest Rate Instruments:

In February 1998, the Company entered into interest rate swap agreements with two of its banks for the purpose of managing its exposure to adverse movements in interest rates and lowering the cost of various debt instruments. The Company does not use financial instruments for trading purposes, and is not a party to leveraged derivatives. Pursuant to the swap agreements, the Company exchanged its floating rate interest obligations on \$50,000 notional principal amount for a fixed interest obligation of 5.55% for three years. The differential paid or received on interest rate agreements is recognized as an adjustment to interest expense.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS

## General

The Company operates in two business segments. Scrap Operations collects, processes and recycles steel scrap through facilities in Oregon, Washington, Alaska and California. Additionally, the Company participates, through joint ventures, in the management of 29 scrap collection and processing facilities, including export terminals in Los Angeles, California; Everett, Massachusetts; Portland, Maine; Providence, Rhode Island and Jersey City, New Jersey. Steel Operations operates a mini-mill in Oregon which produces steel reinforcing bar, merchant bar, coiled rebar and wire rod. Mill depots are maintained in California.

## Results of Operations

The Company's revenues and operating results by business segment are summarized below (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	May 31, 1998	May 31, 1997	May 31, 1998	May 31, 1997
	(unaudited)			
REVENUES:				
Scrap Operations:				
Ferrous sales	\$ 40,497	\$ 47,325	\$ 143,361	\$ 132,156
Nonferrous sales	7,998	7,484	20,005	18,944
Other sales	3,672	5,456	12,267	11,738
	-----	-----	-----	-----
Total sales	52,167	60,265	175,633	162,838
Ferrous sales to Steel Operations	(16,430)	(18,161)	(44,546)	(40,909)
Steel Operations	45,181	47,193	137,129	126,667
	-----	-----	-----	-----
Total	\$ 80,918	\$ 89,297	\$ 268,216	\$ 248,596
	=====	=====	=====	=====
INCOME FROM OPERATIONS:				
Scrap Operations	\$ 2,866	\$ 8,261	\$ 13,886	\$ 15,126
Steel Operations	3,137	1,518	5,775	3,712
Joint ventures	1,417	2,720	8,380	4,500
Corporate expense & eliminations	(1,901)	(1,600)	(5,162)	(5,119)
	-----	-----	-----	-----
Total	\$ 5,519	\$ 10,899	\$ 22,879	\$ 18,219
	=====	=====	=====	=====
NET INCOME	\$ 2,569	\$ 8,424	\$ 12,635	\$ 12,583
	=====	=====	=====	=====

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued):

	For the Three Months Ended		For the Nine Months Ended	
	May 31, 1998	May 31, 1997	May 31, 1998	May 31, 1997
	-----	-----	-----	-----
	(unaudited)			
SHIPMENTS:				
SCRAP OPERATIONS				
Ferrous scrap (long tons):				
To Steel Operations	148	149	379	353
To unaffiliated customers	200	221	746	722
	-----	-----	-----	-----
Total	348	370	1,125	1,075
	=====	=====	=====	=====
Export tons	117	177	547	583
	=====	=====	=====	=====
STEEL OPERATIONS				
Finished steel products (short tons)	131	140	392	378
	-----	-----	-----	-----

Revenues. Consolidated revenues for the three months ended May 31, 1998 decreased \$8.4 million (9%) over the same quarter last year. For the nine months ended May 31, 1998, consolidated revenues increased \$19.6 million (8%) over the same period last year. Revenue increases for the nine months ended May 31, 1998 were generated by both Scrap and Steel Operations.

Revenues from Scrap Operations, before intercompany eliminations, decreased \$8.1 million (13%) for the three months ended May 31, 1998, reflecting a decrease in ferrous tons shipped at lower average selling prices. Ferrous scrap revenues decreased \$6.8 million (14%). Average selling prices decreased \$11 to \$117 per ton compared to the quarter ended May 31, 1997. This decrease in average selling price is primarily attributable to the decline in export prices related to the Asian financial crisis. Ferrous tons shipped to Steel Operations decreased 1%. For the nine months ended May 31, 1998, Scrap Operations' revenues, before intercompany eliminations, were \$12.8 million (8%) over the same period last year. The increase is due to a 5% increase in ferrous tons shipped, at a 4% higher average selling price.

For the three months ended May 31, 1998, Steel Operations' revenues decreased by \$2.0 million (4%) to \$45.2 million. The Company's sales of finished steel decreased 9,000 tons, primarily as a result of adverse weather conditions in California. The effect of decreased tonnage shipped was partially offset by an increase in average selling price for finished steel products of \$7 per ton (2%) to \$344 per ton over the same period last year. Revenues also increased due to increased sales of wire rod and coiled rebar. These products were first introduced into the product mix during the third quarter of 1997 and production of these higher priced items has risen steadily since that time. For the three and nine months ended May 31, 1998, the Company sold 12,700 tons and 41,100 tons of these new products, respectively. This compares to 5,300 tons for the three and nine months ended May 31, 1997. For the nine months ended May 31, 1998, revenues from Steel Operations increased 8% to \$137.1 million. Finished steel shipments increased 14,000 tons (4%) to 392,000 tons. Increased tonnage shipped, coupled with a slight increase in selling prices resulted in higher sales for the period. Additionally, a change in product mix to higher priced products contributed to the increase in revenue and average selling price.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued):

Cost of Goods Sold. Overall cost of goods sold decreased \$4.9 million (6%) during the third quarter of fiscal 1998 compared with the third quarter of fiscal 1997. Cost of goods sold as a percentage of revenues increased from 85% to 88%. Gross profit in total decreased by \$3.4 million (26%) primarily as a result of decreases in export prices realized by Scrap Operations. For the nine months ended May 31, 1998, consolidated cost of goods sold increased \$18.1 million, compared with the same period last year. Cost of goods sold as a percentage of revenues increased from 88% to 89% for the same period, and gross profit increased \$1.5 million (5%), due to an increase in scrap and finished steel tons shipped at higher average selling prices.

For the three months ended May 31, 1998, cost of goods sold for Scrap Operations decreased \$2.8 million and increased as a percentage of revenues from 82% to 89%. Scrap Operations' gross profit decreased from \$11 million to \$5.7 million. The decrease was due to the impact of reduced tonnage shipped and lower average selling prices. For the nine months ended May 31, 1998, Scrap Operations' average ferrous scrap cost of goods sold increased 5% to \$112 per ton. Cost of goods sold as a percentage of revenues increased slightly from 86% to 87%. The increase in tonnage and selling prices, offset by increased cost of raw scrap resulted in a \$.7 million (3%) decrease in gross profit to \$22.7 million.

As a part of its acquisition of Proler (Note 5), the Company acquired a tin scrap processing facility in Lathrop, California that was sold in May 1998. The Company had recorded an environmental reserve for the property when it was acquired. The remaining reserve was reversed upon sale of the facility. The sale resulted in a gain of \$1.1 million, of which \$.8 million is recorded as a reduction of cost of goods sold and \$.3 million as gain on sale of assets for the three months ended May 31, 1998.

Steel Operations' cost of goods sold for the third quarter of fiscal 1998 decreased \$3.8 million (9%) to \$41.1 million and decreased as a percentage of revenue from 95% to 91%. The decrease in cost of goods sold is attributable to a decrease in finished steel shipments, a change in the mix of products shipped, and lower scrap prices. Cost of goods sold per ton, excluding billet sales, decreased from \$318 to \$308 per ton. Gross profit increased 78% from \$2.3 million to \$4.1 million as a result of a change in the mix of products shipped and increased plant efficiencies. For the nine months ended May 31, 1998, Steel Operations' average cost of goods sold per ton decreased from \$320 to \$319. Cost of sales as a percentage of revenues dropped from 95% to 94%. These reductions were the result of increased rolling mill efficiencies.

Income from Joint Ventures. The Company's joint ventures generated \$93.9 million of revenues and contributed \$1.4 million to income for the quarter ended May 31, 1998. This compares with \$92.2 million of revenues, and \$2.7 million contribution to income for the same period last year. The Joint Ventures in the Scrap Processing Business shipped 601,000 tons and 619,000 tons for the same periods, respectively. For the nine months ended May 31, 1998, the joint ventures generated \$287.8 million of revenues and contributed \$8.4 million to income. This compares with \$261.8 million of revenues and \$4.5 million contribution to income for the same period last year. The Joint Ventures in the Scrap Processing Business shipped 1.8 million tons for each of the nine months ended May 31, 1998 and 1997. Income from Joint Ventures decreased from \$2.7 million for the quarter ended May 31, 1997 to \$1.4 million for the quarter ended May 31, 1998. The decrease was due primarily to the Joint Ventures in the Scrap Processing business being negatively impacted by the Asian financial crisis. The revenues, contribution to income, and tons shipped for the nine months ended May 31, 1997 in the discussion above include activity which occurred prior to the Company's acquisition of Proler.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued):

The increase in income from joint ventures fiscal year to date compared to the same period last year is primarily attributable to the Proler joint ventures, which the company acquired in November 1996. Income for the nine months ended May 31, 1997 includes only six months of earnings from these operations.

Export Sales. The Company to date has been able to ship and receive payment for all export sales that it has booked and it anticipates this will continue to be the case. However, the Company has experienced, and for the near term expects to experience, reduced margins on export sales. Selling prices for export scrap to Asia have dropped over \$40 per ton since the first of the fiscal year, and while the Company is adjusting buying prices, it has not yet been able to drop the buying price enough to make up for the drop in selling prices. Additionally, the Company continues to see softening in demand for scrap in certain regions of Asia.

In addition to lowering its scrap purchase price, the Company has increased its domestic sales volume and has begun selling to Asian countries it has not historically sold to. Concurrently, the Company has implemented a variety of cost control measures. With the increased emphasis on domestic sales, the Company believes that fiscal 1998 sales to Asia will be less than 60% of tonnage sold, which has been the average over the last several years. The Company's Joint Ventures in the Scrap Processing Business are less dependent upon Asian sales, expecting to ship approximately 45% of total tonnage to Asia this fiscal year. The Company believes the joint ventures in the Northeast are particularly well positioned over the next several years to take advantage of increasing capacity and demand for scrap in the steel producing areas in the Eastern United States.

While the Company cannot predict how long the Asian crisis will impact its business operations, it believes that the factors cited above will serve to help minimize the financial impact.

Other Income (Expense). In February 1997, the Company entered into an interest rate agreement for the sole purpose of locking in the interest rate on a planned private placement of debt. The Company decided against pursuing the private placement in April 1997, and thus recognized the deferred gain on the agreement of approximately \$3 million. This amount is included in other income in the accompanying statement of operations for the three and nine months ended May 31, 1997.

Interest Expense. Interest expense increased from \$1.5 million for the three months ended May 31, 1997 to \$1.8 million for the same period this year primarily as a result of higher average borrowings. For the nine months ended May 31, 1998, compared to the same period last year, interest expense increased \$.9 million to \$4.5 million. This occurred because average borrowings in the first quarter of 1998 were higher than during the first quarter of 1997, primarily as a result of the Proler acquisition.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued):

Year 2000. The Company continues to assess the potential impact that the Year 2000 issue will have on its reporting systems and operations. The Company has determined that the operating and financial software systems it is currently implementing are Year 2000 compliant. The Company will test new systems for Year 2000 compliance as they are implemented. Additionally, the Company does not believe that the cost of bringing any of its retained software into year 2000 compliance will be material. The Company does not believe that it is substantially reliant on any one customer or supplier and therefore does not believe that the Year 2000 compliance of such companies will have a significant impact on the Company. The Company does not anticipate that the Year 2000 issue will have a significant impact on its financial position or results of operations.

Liquidity and Capital Resources. Cash used by operations for the nine months ended May 31, 1998 was \$140,000, compared with cash provided of \$5.1 million for the same period last year. The decrease in cash flow is primarily attributable to the growth in inventories and a reduction in accounts payable compared to the same period last year.

Capital expenditures for the three months ended May 31, 1998 totaled \$2.8 million compared with \$2.4 million during the same period last year. For the nine months ended May 31, 1998 and 1997, capital expenditures totaled \$7.5 million and \$10.5 million, respectively. The Company anticipates spending approximately \$3.5 million on capital expenditures during the remainder of fiscal 1998.

As a result of certain acquisitions, the Company carries environmental reserves totaling \$28.2 million. The Company expects to require significant future cash outlays as it incurs the actual costs related to the remediation of such environmental liabilities.

As of May 31, 1998, the Company had an unsecured revolving line of credit totaling \$200 million maturing in 2002. The Company had additional unsecured lines of credit available of \$55 million, of which \$20 million was committed. In the aggregate, the Company had borrowings outstanding under these lines totaling \$118.8 million at May 31, 1998.

Pursuant to a stock repurchase program announced by the Company in May 1994 and amended in April 1998, the Company is authorized to repurchase up to 1.6 million shares of its stock when the market price of the Company's stock is not reflective of management's opinion of an appropriate valuation of the stock. Management believes that repurchasing shares under these conditions enhances shareholder value. As of May 31, 1998, a total of 448,300 shares had been purchased under this program. During the nine months ended May 31, 1998, the Company repurchased 196,000 shares of its stock for a total of \$5.1 million.

The Company believes that the current cash balance, internally generated funds, and existing credit facilities will provide adequate financing for capital expenditures, working capital, stock repurchases, and debt service requirements for the next twelve months. In the longer term, the Company may seek to finance business expansion, including potential acquisitions, with additional borrowing arrangements or additional equity financing.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued):

Forward Looking Statements. Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Act of 1934, all of which are subject to risks and uncertainties. One can identify these forward looking statements through the use of words such as "expect," "believe," and other words which convey a similar meaning. One can also identify these statements as they do not relate strictly to historical or current facts. They are likely to address the Company's business strategy, financial projections and results and other global factors affecting the Company's financial prospects. An example of this is the current financial crisis facing certain Asian countries and Year 2000 compliance matters. Other factors that could cause actual results to differ materially are the following: supply and demand conditions; the Company's ability to mitigate the effects of the Asian situation and foreign fiscal policies on its profitability; railroad service difficulties; competitive factors and pricing pressures from national steel companies; imports of foreign steel; availability of scrap supply; fluctuations in scrap prices and seasonality of results. One should understand that it is not possible to predict or identify all factors that could cause actual results to differ from the Company's forward looking statements. Consequently, the reader should not consider any such list to be a complete statement of all potential risks or uncertainties. Further, the Company does not assume any obligation to update any forward looking statement.



PART II

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K:

- (a) Exhibits
  - 3.2 Restated Bylaws of the Registrant
- (b) Reports on Form 8-K
  - None

SIGNATURE

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

SCHNITZER STEEL INDUSTRIES, INC.  
(Registrant)

Date: July 15, 1998  
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By: /s/ BARRY A. ROSEN  
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Barry A. Rosen  
Vice President, Finance

ARTICLE I

SHAREHOLDERS MEETINGS AND VOTING

1.1 Annual Meeting. The annual meeting of the shareholders shall be held during the month of January of each year, unless a different date or time is fixed by the Board of Directors and stated in the notice of the meeting. The failure to hold an annual meeting on the date stated herein shall not affect the validity of any corporate action.

1.2 Special Meetings. Special meetings of the share holders, for any purposes, unless otherwise prescribed by statute, may be called by the Chairman of the Board, President, Secretary or the Board of Directors and shall be called by the Chairman of the Board, President or Secretary upon the written demand, describing the purposes for which the meeting is to be held, signed, dated and delivered to the Secretary, of the holders of not less than one-tenth of all the votes entitled to be cast on any issue proposed to be considered at the meeting.

1.3 Place of Meetings. Meetings of the shareholders shall be held at any place in or out of Oregon designated by the Board of Directors. If a meeting place is not designated by the Board of Directors, the meeting shall be held at the Corporation's principal office.

1.4 Notice of Meetings. Written or printed notice stating the date, time and place of the meeting and, in the case of a special meeting or a meeting for which special notice is required by law, the purposes for which the meeting is called shall be mailed by the Corporation to each shareholder entitled to vote at the meeting and, if required by law, to any other shareholders entitled to receive notice, at the shareholder's address shown in the Corporation's record of shareholders, with postage prepaid, not less than 10 nor more than 60 days before the meeting date, either personally or by mail, by or at the direction of the President, Secretary, or Assistant Secretary, or the officer or persons calling the meeting, to each shareholder of record entitled to vote at such meeting. Notice shall be effective when mailed if it is mailed postpaid and is correctly addressed to the shareholder's address as it appears on the stock transfer books of the Corporation.

1.5 Waiver of Notice. A shareholder may at any time waive any notice required by law, these Bylaws or the Corporation's Articles of Incorporation. The waiver shall be in writing, be

signed by the shareholder entitled to the notice and be delivered to the Corporation for inclusion in the minutes for filing with the corporate records. A shareholder's attendance at a meeting waives objection to (i) lack of notice or defective notice of the meeting, unless the shareholder at the beginning of the meeting objects to holding the meeting or transacting business at the meeting, and (ii) consideration of a particular matter at the meeting that is not within the purposes described in the meeting notice, unless the shareholder objects to considering the matter when it is presented.

1.6 Fixing of Record Date. The Board of Directors may fix a future date as the record date to determine the shareholders entitled to notice of a shareholders' meeting, demand a special meeting, vote, take any other action or receive payment of any share or cash dividend or other distribution. This date shall not be more than 70 days nor, in the case of a meeting, less than 10 days before the meeting or action requiring a determination of shareholders. The record date for any meeting, vote or other action of the shareholders shall be the same for all voting groups. If not otherwise fixed by the Board of Directors, the record date to determine shareholders entitled to notice of and to vote at an annual or special shareholders' meeting is the close of business on the day before the first notice is first mailed or delivered to a shareholder. If not otherwise fixed by the Board of Directors, the record date to determine shareholders entitled to receive payment of any share or cash dividend or other distribution is the close of business on the day the Board of Directors authorizes the share or cash dividend or other distribution.

1.7 Shareholders' List for Meeting. After a record date for a meeting is fixed, the Corporation shall prepare an alphabetical list of all shareholders entitled to notice of the shareholders' meeting. The list shall be arranged by voting group and within each voting group by class or series of shares and show the address of and number of shares held by each shareholder. The shareholders' list shall be available for inspection by any shareholder, upon proper demand as may be required by law, beginning two business days after notice of the meeting is given and continuing through the meeting, at the Corporation's principal office or at a place identified in the meeting notice in the city where the meeting will be held. The Corporation shall make the shareholders' list available at the meeting, and any shareholder or the shareholder's agent or attorney shall be entitled to inspect the list at any time during the meeting or any adjournment. Refusal or failure to prepare or make available the shareholders' list does not affect the validity of action taken at the meeting.

#### 1.8 Quorum; Adjournment.

(1) Shares entitled to vote as a separate voting group may take action on a matter at a meeting only if a quorum of those shares exists with respect to that matter. A majority of the votes entitled to be cast on the matter by the voting group constitutes a quorum of that voting group for action on that matter.

(2) A majority of votes represented at the meeting, although less than a quorum, may adjourn the meeting from time to time to a different time and place without further notice to any shareholder of any adjournment. At an adjourned meeting at which a quorum is present, any business may be transacted that might have been transacted at the meeting originally held.

(3) Once a share is represented for any purpose at a meeting, it shall be present for quorum purposes for the remainder of the meeting and for any adjournment of that meeting unless a new record date is or must be set for the adjourned meeting. A new record date must be set if the meeting is adjourned to a date more than 120 days after the date fixed for the original meeting.

#### 1.9 Voting Requirements; Action Without Meeting.

(1) If a quorum exists, action on a matter, other than the election of directors, by a voting group is approved if the votes cast within the voting group favoring the action exceed the votes cast opposing the action, unless a greater number of affirmative votes is required by law or the Articles of Incorporation. Unless otherwise provided in the Articles of Incorporation, directors are elected by a plurality of the votes cast by the shares entitled to vote in the election at a meeting at which a quorum is present.

(2) Action required or permitted by law to be taken at a shareholders' meeting may be taken without a meeting if the action is taken by all the shareholders entitled to vote on the action. The action must be evidenced by one or more written consents describing the action taken, signed by all the shareholders entitled to vote on the action and delivered to the Secretary for inclusion in the minutes for filing with the corporate records. Shareholders' action taken by written consent is effective when the last shareholder signs the consent, unless the consent specifies an earlier or later effective date.

1.10 Proxies. A shareholder may vote shares in person or by proxy. A shareholder may appoint a proxy by signing an appointment form either personally or by the shareholder's attorney-in-fact. An appointment of a proxy is effective when received by the Secretary or other officer of the Corporation

authorized to tabulate votes. An appointment is valid for 11 months unless a different period is provided in the appointment form. An appointment is revocable by the shareholder unless the appointment form conspicuously states that it is irrevocable and the appointment is coupled with an interest that has not been extinguished.

## ARTICLE II

### BOARD OF DIRECTORS

2.1 Duties of Board of Directors. All corporate powers of the Corporation shall be exercised by or under the authority of its Board of Directors; the business and affairs of the Corporation shall be managed under the direction of its Board of Directors.

2.2 Number, Term and Qualification. The number of directors of the Corporation shall be at least three and no more than thirteen. Within this range, the number of directors shall be determined from time to time by the Board of Directors. The term of a director shall expire at the next annual meeting of shareholders after his or her election. No reduction in the number of directors shall shorten the term of any incumbent director. Despite the expiration of a director's term, the director shall continue to serve until the director's successor is elected and qualified or the number of directors is decreased. Directors need not be residents of Oregon or shareholders of the Corporation.

2.3 Board Member Nominating Committee. When there is a vacancy on the Board of Directors to be filled by the Board, the Chairman of the Board shall appoint a Board Member Nominating Committee consisting of three Board members. The Board Member Nominating Committee will make recommendations to the Board as to nominees qualified to fill the vacancy on the Board. In making its recommendations, the Board Member Nominating Committee will take into account Board membership qualification criteria established by the Board.

2.4 Regular Meetings. A regular meeting of the Board of Directors shall be held without notice other than this Bylaw immediately after, and at the same place as, the annual meeting of shareholders. The Board of Directors may provide by resolution the time and place for the holding of additional regular meetings in or out of Oregon without other notice than the resolution.

2.5 Special Meetings. Special meetings of the Board of Directors may be called by or at the request of the Chairman of the Board, the President or any two directors. The person or

persons authorized to call special meetings of the Board of Directors may fix any place in or out of Oregon as the place for holding any special meeting of the Board of Directors called by them.

2.6 Notice. Notice of the date, time and place of any special meeting of the Board of Directors shall be given at least three days prior to the meeting by notice communicated in person, by telephone, telegraph, teletype, other form of wire or wireless communication, mail or private carrier. If written, notice shall be effective at the earliest of (a) when received, (b) five days after its deposit in the United States mail, as evidenced by the postmark, if mailed postpaid and correctly addressed, or (c) on the date shown on the return receipt, if sent by registered or certified mail, return receipt requested and the receipt is signed by or on behalf of the addressee. Notice by all other means shall be deemed effective when received by or on behalf of the director. Notice of any regular or special meeting need not describe the purposes of the meeting unless required by law or the Articles of Incorporation.

2.7 Waiver of Notice. A director may at any time waive any notice required by law, these Bylaws or the Articles of Incorporation. Except as set forth below, the waiver must be in writing, be signed by the director entitled to the notice, specify the meeting for which notice is waived and be filed with the minutes or corporate records. A director's attendance at or participation in a meeting waives any required notice to the director of the meeting unless the director at the beginning of the meeting, or promptly upon the director's arrival, objects to holding the meeting or transacting business at the meeting and does not thereafter vote for or assent to action taken at the meeting.

2.8 Quorum. A majority of the number of directors fixed in accordance with Section 2.2 of these Bylaws shall constitute a quorum for the transaction of business at any meeting of the Board of Directors. If less than a quorum is present at a meeting, a majority of the directors present may adjourn the meeting from time to time without further notice.

2.9 Manner of Acting. The act of the majority of the directors present at a meeting at which a quorum is present shall be the act of the Board of Directors, unless a different number is provided by law, the Articles of Incorporation or these Bylaws.

2.10 Meeting by Telephone Conference; Action Without Meeting.

(1) Directors may participate in a regular or special meeting by, or conduct the meeting through, use of any means of

communications by which all directors participating may simultaneously hear each other during the meeting. Participation in a meeting by this means shall constitute presence in person at the meeting.

(2) Any action that is required or permitted to be taken at a meeting of the Board of Directors may be taken without a meeting if one or more written consents describing the action taken are signed by all of the directors entitled to vote on the matter and included in the minutes or filed with the corporate records reflecting the action taken. The action shall be effective when the last director signs the consent, unless the consent specifies an earlier or later effective date.

2.11 Vacancies. Any vacancy on the Board of Directors, including a vacancy resulting from an increase in the number of directors, may be filled by the shareholders, the Board of Directors, the remaining directors if less than a quorum (by the affirmative vote of a majority thereof) or by a sole remaining director. Any vacancy not filled by the directors shall be filled by election at an annual meeting or at a special meeting of shareholders called for that purpose. A vacancy that will occur at a specified later date, by reason of a resignation or otherwise, may be filled before the vacancy occurs, but the new director may not take office until the vacancy occurs.

2.12 Compensation. By resolution of the Board of Directors, the directors may be paid reasonable compensation for services as directors and their expenses of attending meetings of the Board of Directors. No such payment shall preclude any director from serving the Corporation in any other capacity and receiving compensation for such service.

2.13 Presumption of Assent. A director who is present at a meeting of the Board of Directors or a committee of the Board of Directors shall be deemed to have assented to the action taken at the meeting unless (a) the director's dissent or abstention from the action is entered in the minutes of the meeting, (b) the director delivers a written notice of dissent or abstention to the action to the presiding officer of the meeting before any adjournment or to the Corporation immediately after the adjournment of the meeting or (c) the director objects at the beginning of the meeting or promptly upon the director's arrival to the holding of the meeting or transacting business at the meeting. The right to dissent or abstain is not available to a director who voted in favor of the action.

2.14 Resignation. Any director may resign by delivering written notice to the Board of Directors, its chairperson or the Corporation. Unless the notice specifies a later effective date, a resignation notice shall be effective upon the earlier of (a) receipt, (b) five days after its deposit in the United States

mails, if mailed postpaid and correctly addressed, or (c) on the date shown on the return receipt, if sent by registered or certified mail, return receipt requested, and the receipt is signed by addressee. Once delivered, a resignation notice is irrevocable unless revocation is permitted by the Board of Directors.

#### ARTICLE III

##### COMMITTEES OF THE BOARD

3.1 Committees. The Board of Directors may create one or more committees and appoint members of the Board of Directors to serve on them. Each committee shall have two or more members. The creation of a committee and appointment of members to it must be approved by a majority of all directors in office when the action is taken. Subject to any limitation imposed by the Board of Directors or by law, each committee may exercise all the authority of the Board of Directors in the management of the Corporation. A committee may not take any action that a committee is prohibited from taking by the Oregon Business Corporation Act, including ORS 60.354 or any successor provision.

3.2 Changes of Size and Function. Subject to the provisions of law, the Board of Directors shall have the power at any time to change the number of committee members, fill committee vacancies, change any committee members and change the functions and terminate the existence of a committee.

3.3 Conduct of Meetings. Each committee shall conduct its meetings in accordance with the applicable provisions of these Bylaws relating to meetings and action without meetings of the Board of Directors. Each committee shall adopt any further rules regarding its conduct, keep minutes and other records and appoint subcommittees and assistants as it deems appropriate.

3.4 Compensation. By resolution of the Board of Directors, committee members may be paid reasonable compensation for services on committees and their expenses of attending committee meetings.

#### ARTICLE IV

##### OFFICERS

4.1 Appointment. The Board of Directors at its first meeting following its election each year shall appoint a President and a Secretary. At this meeting, or at any other time, the Board of Directors may appoint one of its members as Chairman of the Board and one or more Vice Presidents and a Treasurer. The Board of Directors also may appoint any other officers, assistant officers and agents it deems necessary or



appropriate. Any two or more offices may be held by the same person.

4.2 Compensation. The Corporation may pay its officers reasonable compensation for their services as fixed from time to time by resolution of the Board of Directors, and no officer shall be prevented from receiving such salary by reason of the fact that he is also a director of the Corporation.

4.3 Term. The term of office of all officers commences upon their appointment and continues until the first annual meeting of the Board of Directors following their appointment and thereafter until their successors are appointed or until their resignation or removal. Any vacancy in an office of the Corporation may be filled by the Board of Directors.

4.4 Removal. Any officer or agent appointed by the Board of Directors may be removed by the Board of Directors at any time with or without cause, but such removal shall not prejudice the contract rights of the person so removed.

4.5 Chairman of the Board. The Chairman of the Board, if that office is filled, shall preside at all meetings of the Board of Directors and shall perform any duties and responsibilities prescribed from time to time by the Board of Directors, including but not limited to powers and duties similar to those of the President.

4.6 President. The Board of Directors may appoint one or more persons to the Office of the President. One of them shall be designated the chief executive officer of the Corporation who, subject to the control of the Board of Directors, shall in general supervise and control all of the business and affairs of the Corporation. A President shall preside at all meetings of the shareholders and at all meetings of the Board of Directors when the Chairman of the Board of Directors is not present. A President may sign, with the Secretary or any Assistant Secretary, certificates for shares of the Corporation. A President may also sign, with the Secretary or any other officer of the Corporation authorized by the Board of Directors to sign with a President, any deeds, mortgages, bonds, contracts, or other instruments which the Board of Directors has authorized to be executed, except in cases where the Board of Directors or these Bylaws shall expressly delegate the signing and execution of such a document to some other officer or agent of the Corporation or where signing or execution other than by a President as described above shall be required by law. In general, a President shall perform all duties incident to the office of President, and such other duties as may be prescribed by the Board of Directors from time to time.

4.7 Vice Presidents. In the absence of the President or in the event of his death, inability or refusal to act, the Vice President (or in the event there be more than one Vice President, the Vice Presidents in the order designated at the time of their election, or in the absence of any designation, then in the order of their election) shall perform the duties of the president, and when so acting, shall have all the powers of and be subject to all the restrictions upon the President. Any Vice President may sign, with the Secretary or an Assistant Secretary, certificates for shares of the Corporation, and shall perform such other duties as from time to time may be assigned to the Vice President by the President or by the Board of Directors. The Board of Directors or the President may confer a special title upon a Vice President.

4.8 Secretary. The Secretary shall (a) have the responsibility for preparing minutes of the shareholders' and of the Board of Directors' meetings in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provision of these Bylaws or as required by law; (c) be custodian of the corporate records and have the responsibility for authenticating records of the Corporation; (d) be the custodian of the seal of the Corporation and see that the seal of the Corporation is affixed to all documents the execution of which on behalf of the Corporation under its seal is duly authorized; (e) sign with the President, or Vice President, certificates for shares of the Corporation; and (f) in general perform all duties incident to the office of Secretary and such other duties as from time to time may be assigned to the Secretary by the President or by the Board of Directors.

4.9 Treasurer. If required by the Board of Directors, the Treasurer shall give a bond for the faithful discharge of the Treasurer's duties, in such sum and with such security or securities as the Board of Directors shall determine. The Treasurer shall (a) have charge and custody of and be responsible for all funds and securities of the Corporation, (b) receive and give receipts for moneys due and payable to the Corporation from any source whatsoever and (c) deposit all such moneys in the name of the Corporation in such banks, trust companies or other depositories as shall be selected in accordance with the provisions of Article VII of these Bylaws. In general, the Treasurer shall perform all of the duties incident to the office of Treasurer and such other duties as from time to time may be assigned to the Treasurer by the President or by the Board of Directors.

## ARTICLE V

### INDEMNIFICATION

The Corporation shall indemnify, to the fullest extent not prohibited by law, any current or former director or officer of the Corporation who is made, or threatened to be made, a party to an action, suit or proceeding, whether civil, criminal, administrative, investigative or other (including an action, suit or proceeding by or in the right of the Corporation) by reason of the fact that such person is or was a director, officer, employee or agent of the Corporation or a fiduciary within the meaning of the Employee Retirement Income Security Act of 1974 with respect to any employee benefit plan of the Corporation, or serves or served at the request of the Corporation as a director, officer, employee or agent, or as a fiduciary of an employee benefit plan, of another corporation, partnership, joint venture, trust or other enterprise. The Corporation shall pay all expenses incurred by any such person defending such proceeding in advance of its final disposition at the written request of such person if the person furnishes the Corporation (a) a written statement of a good faith belief that he or she is entitled to indemnification and (b) a written undertaking to repay such advance if it is ultimately determined by a court that such person is not entitled to be indemnified. No amendment to these Bylaws that limits the Corporation's obligation to indemnify directors and officers of the Corporation shall have any effect on such obligation for any act or omission which occurs prior to the later of the effective date of the amendment or the date notice of the amendment is given to the officer or director. This Article shall not be deemed exclusive of any other provisions for indemnification or advancement of expenses of directors, officers, employees, agents and fiduciaries that may be included in the Corporation's Articles of Incorporation or any statute, agreement, general or specific action of the Board of Directors, vote of shareholders or other document or arrangement.

## ARTICLE VI

### ISSUANCE OF SHARES

6.1 Adequacy of Consideration. Before the Corporation issues shares, the Board of Directors shall determine that the consideration received or to be received for the shares to be issued is adequate. The authorization by the Board of Directors of the issuance of shares for stated consideration shall evidence a determination by the Board that such consideration is adequate.

## 6.2 Certificates for Shares.

(1) Certificates representing shares of the Corporation shall be in any form determined by the Board of Directors consistent with the requirements of the Oregon Business Corporation Act and these Bylaws. The certificates shall be signed by the President or a Vice President and by the Secretary or an Assistant Secretary and may be sealed with the seal of the Corporation, if any, or a facsimile thereof. All certificates for shares shall be consecutively numbered or otherwise identified. The signatures of officers upon a certificate may be facsimiles if the certificate is countersigned by a transfer agent or any assistant transfer agent or registered by a registrar, other than the Corporation itself or an employee of the Corporation.

(2) Every certificate for shares of stock that are subject to any restriction on transfer or registration of transfer pursuant to the Articles of Incorporation, the Bylaws, securities laws, shareholders' agreements or any agreement to which the Corporation is a party shall have conspicuously noted on the face or back of the certificate either the full text of the restriction or a statement of the existence of the restriction and that the Corporation retains a copy of the full text. Every certificate issued when the Corporation is authorized to issue more than one class or series within a class of shares shall set forth on its face or back either (a) a summary of the designations, relative rights, preferences and limitations of the shares of each class and the variations in rights, preferences and limitations for each series authorized to be issued and the authority of the Board of Directors to determine variations for future series or (b) a statement of the existence of those designations, relative rights, preferences and limitations and a statement that the Corporation will furnish a copy thereof to the holder of the certificate upon written request and without charge.

(3) The name and address of the person to whom the shares represented by the certificates are issued, with the number of shares and the date of issue, shall be entered on the stock transfer books of the Corporation. All certificates surrendered to the Corporation for transfer shall be canceled. The Corporation shall not issue a new certificate for previously issued shares until the former certificate or certificates for those shares are surrendered and canceled; except that in case of a lost, destroyed or mutilated certificate, a new certificate may be issued on terms the Board of Directors prescribes.

6.3 Transfer of Shares. Transfer of shares of the Corporation shall be made only on the stock transfer books of the Corporation by the holder of record of the shares or by the holder's legal representative, who shall furnish proper evidence

of authority to transfer, or by the holder's attorney with regard to the shares authorized by a duly executed power of attorney filed with the Secretary or the transfer agent of the Corporation, and on surrender for cancellation for such shares. The Corporation shall deem the person in whose name shares stand on the books of the Corporation to be the owner of those shares for all purposes.

6.4 Transfer Agent and Registrar. The Board of Directors may from time to time appoint one or more transfer agents and one or more registrars for the shares of the Corporation, with powers and duties determined by the Board of Directors.

6.5 Officer Ceasing to Act. If the person who signed a share certificate, either manually or in facsimile, no longer holds office when the certificate is issued, the certificate is nevertheless valid.

#### ARTICLE VII

##### CONTRACTS, LOANS, CHECKS AND OTHER INSTRUMENTS

7.1 Contracts. Except as otherwise provided by law, the Board of Directors may authorize any officers or agents to execute and deliver any contract or other instrument in the name of and on behalf of the Corporation, and this authority may be general or confined to specific instances.

7.2 Loans. The Corporation shall not borrow money and no evidence of indebtedness shall be issued in its name unless authorized by the Board of Directors. This authority may be general or confined to specific instances.

7.3 Checks, Drafts, Etc. All checks, drafts or other orders for the payment of money and notes or other evidences of indebtedness issued in the name of the Corporation shall be signed by the officers or agents of the Corporation and in the manner designated by the Board of Directors.

7.4 Deposits. All funds of the Corporation not otherwise employed shall be deposited to the credit of the Corporation in those banks, trust companies or other depositories as the Board of Directors or officers of the Corporation designated by the Board of Directors select or be invested as authorized by the Board of Directors.

ARTICLE VIII

MISCELLANEOUS PROVISIONS

8.1 Fiscal Year. The business of the Corporation shall be conducted on a fiscal year basis beginning with the first day of September and ending on the last day of August of each year.

8.2 Dividends. The Board of Directors may from time to time declare, and the Corporation may pay, dividends on its outstanding shares, in the manner and upon the terms and conditions provided by law.

8.3 Seal. The Board of Directors shall provide a corporate seal which shall be circular in form and shall have inscribed thereon the name of the Corporation and the words "Corporate Seal, Oregon."

8.4 Severability. A determination that any provision of these Bylaws is for any reason inapplicable, invalid, illegal or otherwise ineffective shall not affect or invalidate any other provision of these Bylaws.

8.5 Amendments. Except as restricted by the Corporation's Articles of Incorporation, these Bylaws may be amended or repealed and new Bylaws may be adopted by the Board of Directors or the shareholders of the Corporation.

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONSOLIDATED BALANCE SHEET AND THE CONSOLIDATED STATEMENT OF OPERATIONS FILED AS PART OF THE QUARTERLY REPORT ON FORM 10-Q AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

1,000

9-MOS		9-MOS	
AUG-31-1997		AUG-31-1998	
SEP-01-1996		SEP-01-1997	
MAY-31-1997		MAY-31-1998	
	0		1,666
	0		0
	0		31,027
	0		485
	0		104,506
0		154,285	
	0		267,508
	0		124,583
	0		463,022
0		34,453	
	0		128,988
0		0	
	0		0
	0		9,986
	0		235,137
0	463,022		
	248,596		268,216
248,596		268,216	
	219,434		237,746
	234,877		253,717
(4,441)		(1,096)	
63		(113)	
3,583		4,537	
19,077		19,438	
6,494		6,803	
12,583		12,635	
	0		0
	0		0
	0		0
	12,583		12,635
	1.22		1.25
	1.21		1.25

The restated balance sheet as of May 31, 1997 is not included in this report.