# BRUSH ENGINEERED MATERIALS INC 

FORM 10-Q<br>(Quarterly Report)

Filed 11/13/2001 For Period Ending 9/28/2001

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| :--- | :--- |
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| CIK | 0001104657 |
| Industry | Metal Mining |
| Sector | Basic Materials |
| Fiscal Year | $12 / 31$ |

# UNITED STATES SECURITIES AND EXCHANGE <br> COMMISSION <br> 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 September 28, 2001

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 1-7006

## BRUSH ENGINEERED MATERIALS INC. <br> (EXACT NAME OF REGISTRANT AS SPECIFIED IN CHARTER)

OHIO<br>(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)<br>17876 ST. CLAIR AVENUE, CLEVELAND, OHIO<br>(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

44110

216-486-4200
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 [X] No [ ]

As of November 2, 2001 there were $16,610,755$ shares of Common Stock, no par value, outstanding.

## PART I FINANCIAL INFORMATION

## BRUSH ENGINEERED MATERIALS INC. AND SUBSIDIARIES

## ITEM 1. FINANCIAL STATEMENTS

The consolidated financial statements of Brush Engineered Materials Inc. (formerly Brush Wellman Inc.) and its subsidiaries for the quarter ended September 28, 2001 are as follows:

Consolidated Statements of Income -- Three and nine months ended September 28, 2001 and September 29, 2000

Consolidated Balance Sheets --
September 28, 2001 and December 31, 2000

Consolidated Statements of Cash Flows -- Nine months ended September 28, 2001 and September 29, 2000

## CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

| (Dollars in thousands except share and per share amounts) | THIRD QUARTER ENDED |  |  |  | NINE MONTHS ENDED |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | SEPT. 28, 2001 |  | SEPT. 29, 2000 |  | SEPT. 28, 200 |  | SEPT. 29, 200 |  |
| Net sales. | \$ | 106,194 | \$ | 143,926 | \$ | 380,174 | \$ | 416,532 |
| Cost of sales |  | 98,941 |  | 115,304 |  | 315,311 |  | 329,912 |
| Gross Margin. |  | 7,253 |  | 28,622 |  | 64,863 |  | 86,620 |
| Selling, general and administrative expenses.......................... |  | 17,700 |  | 21,101 |  | 57,977 |  | 64,065 |
| Research and development expenses. |  | 1,416 |  | 1,870 |  | 4,975 |  | 5,571 |
| Other-net |  | $(1,128)$ |  | (19) |  | (103) |  | 314 |
| Operating (Loss) Profit |  | $(10,735)$ |  | 5,670 |  | 2,014 |  | 16,670 |
| Interest expense. |  | 679 |  | 1,227 |  | 2,507 |  | 3,407 |
| (Loss) Income before income taxes |  | $(11,414)$ |  | 4,443 |  | (493) |  | 13,263 |
| Income taxes. |  | $(3,647)$ |  | 359 |  | (207) |  | 3,032 |
| Net (Loss) Income. | \$ | $(7,767)$ | \$ | 4,084 | \$ | (286) | \$ | 10,231 |
| Weighted average number of common shares outstanding.................. | \$ | (0.47) | \$ | 0.25 | \$ | (0.02) | \$ | 0.63 |
|  | 16,548,410 |  | 16,315,523 |  | 16,508,784 |  | 16,248,733 |  |
| Per Share of Common Stock: Diluted. | \$ | (0.47) | \$ | 0.25 | \$ | (0.02) | \$ | 0.62 |
| Weighted average number of common shares outstanding............. | 16,548,410 | ,548,410 | 16,521,028 |  | 16,508,784 |  | 16,392,435 |  |
| Cash dividends per common share | \$ | -- | \$ | 0.12 | \$ | 0.24 | \$ | 0.36 |

See notes to consolidated financial statements.
(UNAUDITED)


See notes to consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)


See notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

## NOTE A -- ACCOUNTING POLICIES

In management's opinion, the accompanying consolidated financial statements contain all adjustments necessary to present fairly the financial position as of September 28, 2001 and December 31, 2000 and the results of operations for the third quarter ended September 28, 2001 and September 29, 2000. All of the adjustments were of a normal and recurring nature.

## NOTE B -- INVENTORIES

| (Dollars in thousands) | $\begin{gathered} \text { SEPTEMBER } 28, \\ 2001 \end{gathered}$ | $\begin{gathered} \text { DECEMBER } 31 \\ 2000 \end{gathered}$ |
| :---: | :---: | :---: |
| Principally average cost: |  |  |
| Raw materials and supplies | \$ 18,371 | \$ 19,458 |
| In process | 82,337 | 88,956 |
| Finished goods | 44,775 | 33,202 |
| Gross inventories. | 145,483 | 141,616 |
| Excess of average cost over LIFO |  |  |
| Inventory value. | 26,503 | 25,973 |
| Net inventories | \$118,980 | \$115,643 |

## NOTE C -- COMPREHENSIVE INCOME

The reconciliation between Net Income and Comprehensive Income for the three and nine month periods ending September 28, 2001 and September 29, 2000 is as follows:


## NOTE D -- SEGMENT REPORTING

As a result of the recent corporate restructuring, the Company changed how costs flowed between its businesses. Certain costs that were previously included in the "All Other" column in the segment disclosures are being charged to Metal Systems and Microelectronics beginning in the first quarter 2001. Beginning in 2001, the "All Other" column includes the operating results of BEM Services Inc. and Brush Resources Inc., two wholly-owned subsidiaries of the Company, as well as the parent company's operating expenses. BEM Services charges a management fee for the services provided to the other businesses within the Company on a cost-plus basis. Brush Resources may sell beryllium hydroxide, produced from its mine and extraction mill in Utah, to outside
customers and to businesses within the Metal Systems Group. Segment results from the prior year have been restated to reflect these changes on a pro forma basis.

| (Dollars in thousands) | METAL SYSTEMS | MICROELECTRONICS | TOTAL SEGMENTS | $\begin{aligned} & \text { ALL } \\ & \text { OTHER } \end{aligned}$ | TOTAL |
| :---: | :---: | :---: | :---: | :---: | :---: |
| THIRD QUARTER 2001 |  |  |  |  |  |
| Revenues from external customers | \$ 61,778 | \$ 41,656 | \$103,434 | \$2,760 | \$106,194 |
| Intersegment revenues | 578 | 542 | 1,120 | 1,311 | 2,431 |
| Profit (loss) before interest and taxes. | $(9,393)$ | 208 | $(9,185)$ | $(1,550)$ | $(10,735)$ |
| THIRD QUARTER 2000 |  |  |  |  |  |
| Revenues from external customers | \$ 93,917 | \$ 48,498 | \$142,415 | \$1,511 | \$143,926 |
| Intersegment revenues | 748 | 553 | 1,301 | 5,239 | 6,540 |
| Profit (loss) before interest and taxes | 3,572 | 3,042 | 6,614 | (944) | 5,670 |
| FIRST NINE MONTHS 2001 |  |  |  |  |  |
| Revenues from external customers | \$243,809 | \$130,851 | \$374,660 | \$5,514 | \$380,174 |
| Intersegment revenues | 2,516 | 1,843 | 4,359 | 11,697 | 16,056 |
| Profit (loss) before interest and taxes. | $(4,445)$ | 3,548 | (897) | 2,911 | 2,014 |
| FIRST NINE MONTHS 2000 |  |  |  |  |  |
| Revenues from external customers | \$280,181 | \$131,923 | \$412,104 | \$4,428 | \$416,532 |
| Intersegment revenues. | 3,326 | 1,079 | 4,405 | 16,272 | 20,677 |
| Profit (loss) before interest and taxes. | 5,817 | 7,843 | 13,660 | 3,010 | 16,670 |

## NOTE E -- DERIVATIVE FINANCIAL INSTRUMENTS

The Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and as amended by SFAS No. 138 "Accounting for Certain Derivative Instruments and Certain Hedging Activities" as of January 1, 2001. The initial adjustment from adopting SFAS Nos. 133 (as amended) did not have a material impact on earnings and resulted in a $\$ 0.4$ million charge recorded against other comprehensive income on the balance sheet.

The Company is exposed to commodity price, interest rate and foreign currency exchange rate risks and attempts to minimize the effects of these exposures on earnings through a combination of natural hedges and the use of derivative financial instruments. The Company may secure commodity swaps to hedge copper purchases where changes in the copper price cannot be passed through to the Company's customers. The Company uses interest rate swaps to fix interest rates on floating rate obligations as appropriate. The Company also uses forward contracts, options and collars to hedge a portion of its anticipated foreign currency transactions. The Company has policies approved by the Board of Directors that establish the parameters for the allowable types of derivative instruments to be used, the maximum allowable contract periods, aggregate dollar limitations and other hedging guidelines. The Company will only secure a derivative if there is an identifiable underlying exposure that is not otherwise covered by a natural hedge. In general, derivatives will be held until maturity.

All of the Company's commodity swaps, interest rate swaps and foreign currency derivatives have been designated as cash flow hedges. Hedge ineffectiveness of $\$ 44,000$ was charged against income in the first nine months of 2001 , including $\$ 26,000$ in the third quarter, and was included in other-net on the Company's consolidated statements of income. All commodity swaps and foreign currency derivatives outstanding as of September 28, 2001 mature prior to December 31, 2002.

SFAS No. 133 requires the fair value of outstanding derivative instruments to be recorded on the balance sheet. With the adoption of SFAS No. 133, the Company began recording the fair values of its derivatives in prepaid expenses, other assets, other liabilities and accrued items and other long-term liabilities depending on the Company's rights or obligations under each derivative and the remaining term to maturity. As of September 28, 2001, the Company recorded derivative fair values of $\$ 1.5$ million in prepaid expenses, $\$ 0.3$ million in other assets, $\$ 2.8$ million in other liabilities and accrued items and $\$ 3.9$ million in other long-term liabilities on its
consolidated balance sheet. Changes in fair values are recorded in income or other comprehensive income as appropriate under SFAS No. 133 guidelines. The change in the fair value of the Company's outstanding derivatives and other current hedging activity resulted in a debit to other comprehensive income of $\$ 6.1$ million in the third quarter 2001 and $\$ 6.1$ million for the first nine months of 2001. The majority of the change in the third quarter resulted from the revaluation of a long-term variable-to-fixed interest rate swap and the revaluation of variable-to-fixed copper price swaps. As a result of derivatives maturing, $\$ 0.6$ million was relieved from other comprehensive income and charged to income in the third quarter 2001 while $\$ 1.0$ million was charged out of other comprehensive income against net income during the first nine months of 2001. The net derivative loss recorded in other comprehensive income was $\$ 5.5$ million as of September 28, 2001. The Company expects to reclassify $\$ 0.7$ million of net gain on derivative instruments from the initial adjustment to other comprehensive income to earnings during the year ending December 31, 2001.

The Company hedges a portion of its net investment in its Japanese subsidiary using yen denominated debt. A net loss of $\$ 0.1$ million associated with translating this debt into dollars was recorded in the cumulative translation adjustment as of September 28, 2001.

## NOTE F -- NEW PRONOUNCEMENT

In June 2001, the Financial Standards Accounting Board issued Statement No. 142, "Goodwill and Other Intangible Assets". Under this statement, goodwill and other indefinite lived assets will no longer be amortized, but instead will be reviewed annually, or more frequently under certain circumstances, for impairment. Intangible assets with finite lives will continue to be amortized over their useful lives. The amortization provisions of the statement apply to any goodwill or other intangible assets acquired after June 30, 2001. The amortization provisions do not apply to goodwill and other intangible assets acquired prior to July 1,2001 until adoption of the statement. The Company is required to adopt the statement by January 1, 2002, but early adoption is allowed. The Company had goodwill of $\$ 7.9$ million on its consolidated balance sheet as of September 28, 2001.

## NOTE G -- FINANCING ARRANGEMENTS

The Company received a waiver from its bank group for certain covenants contained in its $\$ 65.0$ million revolving credit agreement and its $\$ 59.7$ million synthetic lease as of September 28, 2001. The banks agreed to waive the fixed charge coverage ratio and the funded debt to EBITDAR (earnings before interest, taxes, depreciation, amortization and certain rent obligations) ratio covenants through the end of the third quarter 2002. As part of the waiver, the banks took a security interest in the Company's domestic assets. The banks and the Company also agreed to discuss amending these agreements during the fourth quarter 2001. The outstanding borrowings under the revolving credit agreement totaled $\$ 46.9$ million as of September 28, 2001. The synthetic lease is considered an operating lease and therefore is an off-balance sheet obligation.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

## FORWARD LOOKING STATEMENTS

Portions set forth in this document that are not statements of historical or current facts are forward-looking statements. The Company's actual future performance may materially differ from that contemplated by the forward-looking statements as a result of a variety of factors. These factors include, in addition to those mentioned elsewhere herein, the condition of the markets which the Company serves (especially as impacted by events in particular markets, including telecommunications, automotive electronics, computers, optical media and microelectronics, or in particular geographic regions), the Company's success in implementing its strategic plans, the timely and successful completion of pending capital expansion projects, the realization of savings from cost reduction initiatives, possible changes in government regulatory requirements, the enactment of new legislation that impacts the Company's obligations and the conclusion of pending litigation matters in accordance with the Company's expectation that there will be no material adverse effects.

## RESULTS OF OPERATIONS



Sales of $\$ 106.2$ million in the third quarter 2001 were $26 \%$ lower than sales in the third quarter 2000. Sales have declined for three straight quarters after establishing record highs in each of the previous five quarters. Sales for the first nine months of 2001 of $\$ 380.2$ million were $9 \%$ lower than the comparable period in 2000. The sales fall-off in both the current quarter and the year was mainly due to softening of demand from the Company's two largest markets -- telecommunications and computer electronics. Demand from several of the Company's other markets also declined in the third quarter. Sales from both of the Company's reportable business segments -- the Metal Systems Group and the Microelectronics Group (MEG) -- were lower in the third quarter 2001 than in the third quarter 2000. The fall-off in demand had the largest effect on Alloy Products and Technical Materials, Inc. within the Metal Systems Group and Electronic Products within the MEG.

The slow down in sales occurred predominately in the domestic portion of the business earlier in the year, with the international sales slow down occurring in the third quarter. International sales were $\$ 30.6$ million ( $28.9 \%$ of sales) in the third quarter 2001 compared to $\$ 35.7$ million ( $24.8 \%$ of sales) in the third quarter 2000. For the first three quarters, international sales were $\$ 110.8$ million in 2001 and $\$ 111.8$ million in 2000. The Company's sales from its international service centers are denominated in foreign currencies, primarily the euro, yen and sterling. The dollar on average has strengthened in 2001 compared to 2000 , resulting in a lower translated value of these sales. The impact of the exchange rate effect on sales was a negative $\$ 0.8$ million in the third quarter and a negative $\$ 4.1$ million for the first nine months of 2001.

The Company is facing increased pressures to reduce its selling prices in light of the current economic conditions of its major markets. While prices may have been reduced on particular applications in order to maintain the business, average prices in general remain equal to or greater than they were a year ago.

Precious metal prices are typically passed through to the customer so changes in the Company's purchase prices are offset by changes in the sales value with no impact on margins. Sales were $\$ 0.8$ million lower in the third quarter 2001 as compared to the third quarter 2000 as a result of lower average precious metal prices in the current period. For the year, the precious metal prices have reduced sales by $\$ 0.5$ million.

Gross margin in the third quarter 2001 was $\$ 7.3$ million or $6.8 \%$ of sales compared to $\$ 28.6$ million or $19.9 \%$ of sales in the third quarter 2000 . For the first three quarters of 2001, gross margin was $\$ 64.9$ million, a decline of $\$ 21.7$ million from the first three quarters of 2000 , while margin as a percent of sales decreased to $17.1 \%$ from $20.8 \%$. All but $\$ 0.4$ million of the year-to-date margin decline occurred in the third quarter. The main cause of the lower margins in the quarter is the lower sales volume and the related reduced production
volumes. The lower volumes reduced the variable margin contribution (sales less materials and direct manufacturing costs) by $\$ 14.4$ million in the third quarter 2001 from the third quarter 2000. The aforementioned negative currency effect on sales also flowed through against margins, the majority of which was in the Metal Systems Group. The sales mix effect on the third quarter margins was approximately $\$ 0.3$ million unfavorable. The balance of the decline in margins in the current quarter was caused by a combination of an increase in unabsorbed manufacturing costs, inventory reductions and inventory valuation adjustments. Cost reductions were made in the quarter, both in the variable cost and manufacturing overhead areas. However, sales volumes dropped further and faster than anticipated and therefore the cost reduction efforts, particularly in manufacturing overhead, were not commensurate with the declining volumes, which then lead to an increase in unabsorbed costs. Several manufacturing facilities, including the Elmore, OH and Delta, UT plants, reduced their productive output in part by taking longer plant shutdowns in the third quarter of this year as compared to last year. TMI operated on a 32 -hour workweek schedule through out the quarter as part of the cost reduction effort and in order to help balance output with demand.

Selling, general and administrative (SG\&A) expenses were $\$ 17.7$ million, or $16.7 \%$ of sales, in the third quarter 2001, a $\$ 3.4$ million reduction from the third quarter 2000. For the first nine months of the year, SG\&A expenses were $\$ 58.0$ million in 2001 and $\$ 64.1$ million in 2000. SG\&A expenses were $15.3 \%$ of year-to-date 2001 sales, relatively unchanged from the $15.4 \%$ of sales in the first nine months of 2000. The lower expenses in the quarter resulted from cost reduction initiatives, including layoffs, in light of the declining sales volumes. Incentive compensation accruals were also significantly lower than in the comparable quarter last year due to the fall-off in profits. In response to the lower sales volumes, the Company announced the closing of its California distribution center. This facility was the smallest of Alloy Products' four domestic distribution centers and the Company believes that customers can receive the same high quality of service from one of the other distribution centers and/or from its network of independent distributors. One-time shutdown costs for this facility and the severance costs for the layoffs company-wide totaled approximately $\$ 0.8$ million in third quarter 2001 and is included in the $\$ 17.7$ million SG\&A expense. In addition to the above items, the 2001 year-to-date expenses were lower than in 2000 due to non-recurring legal costs associated with the corporate restructuring and miscellaneous law suits in 2000 and lower medical and environmental, health and safety costs in the first half of 2001.

Research and development expenses (R\&D) were $\$ 1.4$ million in the third quarter 2001 and $\$ 1.9$ million in the third quarter 2000. For the first nine months, $R \& D$ expenses were $\$ 5.0$ million in 2001 and $\$ 5.6$ million in 2000 . As a percent of sales, R\&D expenses remain unchanged at $1.3 \%$. The spending level within R\&D has been reduced as part of the Company's over-all cost reduction effort.

Other-net income was $\$ 1.1$ million in the third quarter 2001 compared to less than $\$ 0.1$ million in the third quarter 2000. The metal financing fee on precious metal and copper inventories was lower in the third quarter 2001 than the third quarter 2000. In addition, accruals were reduced $\$ 0.6$ million on an environmental remediation project in the third quarter 2001 as a result of revised cost estimates. For the first nine months of the year, Other-net income was $\$ 0.1$ million in 2001 versus a net expense of $\$ 0.3$ million in 2000. The year-to-date metal financing fee is lower in 2001, offsetting a reduction in the year-to-date currency exchange gains. Other-net also includes gains and losses on the disposal of fixed assets, amortization of intangible assets, bad debts, cash discounts and other non-operating items.

The operating loss was $\$ 10.7$ million in the third quarter 2001 compared to an operating profit of $\$ 5.7$ million in the third quarter 2000. With the loss in the third quarter, the operating profit for the first nine months of 2001 was reduced to $\$ 2.0$ million while profit in the first nine months of 2000 was $\$ 16.7$ million.

The main cause for the decline in profit is the lower sales and the related impact from reduced production volumes and inventory adjustments, partially offset by lower expenses. Prior to the third quarter, the operating profit in 2001 was $\$ 1.7$ million higher than in the first half of 2000 .

Interest expense was $\$ 0.7$ million in the third quarter 2001 compared to $\$ 1.2$ million in the third quarter 2000. For the year thus far, interest expense was $\$ 2.5$ million in 2001 and $\$ 3.4$ million in 2000 . The lower expense in the third quarter 2001 resulted from a decline in the average borrowing rates as average debt levels were higher in the current quarter. Interest capitalized in association with long-term projects was unchanged
between the third quarter this year and last year, but it was $\$ 0.3$ million higher in the first half of 2001 than in the first half of 2000 .

The loss before income taxes was $\$ 11.4$ million in the third quarter and $\$ 0.5$ million for the first nine months of 2001. In 2000, the Company had income before income taxes of $\$ 4.4$ million in the third quarter and $\$ 13.3$ million in the first nine months.

A tax benefit rate of $32.0 \%$ was applied against the loss before income taxes in the third quarter 2001. The 2001 year-to-date tax benefit rate was $42.0 \%$. The third quarter year-to-date tax rate in 2000 was $22.9 \%$. Since the Company is in a loss position in 2001, normal credits, such as foreign tax benefits and the depletion allowance, increase the tax benefit rate whereas in the prior year these credits served to reduce the rate at which the tax expense was applied.

The net loss was $\$ 7.8$ million in the third quarter 2001 , or $\$ 0.47$ per share, and $\$ 0.3$ million in the first three quarters of 2001 , or $\$ 0.02$ per share. In 2000, the Company earned $\$ 4.1$ million, or $\$ 0.25$ per share, in the third quarter and $\$ 10.2$ million, or $\$ 0.62$ per share, in the first three quarters.

## SEGMENT DISCLOSURES

The Company aggregates its businesses into two reportable segments - the Metal Systems Group and the Microelectronics Group. Corporate expenses as well as the operating results from the Company's beryllium mine and extraction mill in Utah historically were not included in either segment and were shown in the "All Other" column in the segment footnote.

As a result of the recent corporate restructuring, the Company changed how costs flow between its various businesses and the corporate office. Certain costs that previously were recorded at the corporate office, primarily expenses related to beryllium health and safety and chronic beryllium disease, are being charged to the responsible businesses beginning in the first quarter 2001. Beginning in 2001, the "All Other" column in the segment disclosures includes the operating results of BEM Services, Inc. and Brush Resources Inc., two wholly-owned subsidiaries of the Company, as well as the parent company's operating expenses. BEM Services charges a management fee for the services it provides, primarily corporate, administrative and financial over-sight, to the other businesses within the Company on a cost-plus basis. Brush Resources sells beryllium hydroxide, produced through its Utah operations, to outside customers and to businesses within the Metal Systems Group. The 2000 segment results presented in Note D to the Consolidated Financial Statements for the period ended September 28, 2001, as well as in this Management Discussion and Analysis, have been revised to reflect these changes on a pro forma basis. Management believes that these changes should more accurately reflect the operating results of its businesses on a go forward basis.

## METAL SYSTEMS GROUP

|  | THIRD QUARTER |  | FIRST NINE MONTHS |  |
| :---: | :---: | :---: | :---: | :---: |
| (MILLIONS) | 2001 | 2000 | 2001 | 2000 |
| Sales | \$61.8 | \$93.9 | \$243.8 | \$280.2 |
| Operating Profit (Loss) | (9.4) | 3.6 | (4.4) | 5.8 |

Total Metal Systems Group sales declined $\$ 32.1$ million, or $34 \%$, in the third quarter 2001 from the third quarter 2000 while sales for the first nine months of the year declined $\$ 36.4$ million, a $13 \%$ drop from last year. After earning a $\$ 5.0$ million profit in the first half of 2001 , the Group lost $\$ 9.4$ million in the third quarter 2001, mainly as a result of the fall-off in volume.

The Metal Systems Group consists of Alloy Products, TMI and Beryllium Products. The following chart highlights business unit sales as a percent of the total Metal Systems Group sales:

|  | THIRD QUARTER |  | FIRST NINE MONTHS |  |
| :---: | :---: | :---: | :---: | :---: |
|  | 2001 | 2000 | 2001 | 2000 |
| Percent of Segment Sales |  |  |  |  |
| Alloy. | 76.8\% | 69.9\% | $74.5 \%$ | 71.3\% |
| TMI. | 13.7 | 22.9 | 17.0 | 22.5 |
| Beryllium Products | 9.5 | 7.2 | 8.5 | 6.2 |

Sales by Alloy Products, the Company's largest business, decreased $27.7 \%$ in the third quarter 2001 from the third quarter 2000. Year-to-date sales of Alloy Products sales were $9.0 \%$ lower in 2001 than 2000 . After growing $6 \%$ in the first quarter 2001, Alloy sales have now declined two straight quarters. Alloy Products consists of two main product lines - strip products and bulk products. Strip products include precision strip and small diameter rod and wire manufactured from beryllium copper alloys. Sales of these products were $35.7 \%$ lower in the third quarter 2001 and $12.7 \%$ lower in the first three quarters of 2001 than the comparable periods last year as a result of the slow down in telecommunications and computer electronics, strip products' two largest markets. Strip pounds sold were $20 \%$ less in the first nine months of 2001 than in the first nine months of 2000 . Sales order entry rates for strip products continued to be lower than in prior periods and there was no appreciable change in the backlog during the third quarter. Production levels at the Company's strip manufacturing operations at the Elmore, OH and Reading, PA. facilities were reduced once again in response to the lower demand and in order to reduce inventories. During most of 2000, these facilities were capacity constrained and were unable to meet all of the customer demand.

Sales of bulk products declined $9.6 \%$ in the third quarter 2001 from the third quarter 2000 while year-to-date 2001 sales are slightly higher than in 2000. Bulk products include beryllium and non-beryllium copper alloy products manufactured in bar, tube, rod, plate and a variety of customized forms. Sales into the plastic tooling and welding markets continued to lag last year's pace while sales into the oil and gas, aerospace and undersea communications markets slowed in third quarter 2001 after growing in the first half of the current year. Total bulk product pounds sold were $2 \%$ less in the first nine months of 2001 than in the first nine months of 2000.

TMI sales were $60.7 \%$ lower in the third quarter and $34.2 \%$ lower for the first nine months of 2001 than the comparable periods in 2000. Major applications for TMI's products, which are manufactured at the Company's Lincoln, RI facility, include contacts, semiconductors and connectors. The slowdown in the telecommunications and computer electronics markets began impacting sales volumes of these products late in the first quarter 2001. Management believes that the fall-off in these sales is related to the over-all market conditions and not caused by a loss in market share or technological obsolescence. Sales order entry rates showed a mild improvement late in the third quarter 2001. TMI implemented additional cost reduction initiatives in the second and third quarters, including further reductions in force, cost controls and reduced work hours and TMI remained profitable for the year despite the reduced volumes.

Beryllium Products sales in the third quarter 2001 were $13.2 \%$ below the third quarter 2000. However, year-to-date sales have grown $18.9 \%$ over last year. Major markets for these products include defense, medical, optical scanning and electronics. The decline in sales in the third quarter was due to delays in government spending on approved defense programs. The Company anticipates that defense related orders should increase over the next several quarters.

The gross margin on Metal Systems sales was $3.8 \%$ of sales in the third quarter 2001 compared to $20.7 \%$ in the third quarter 2000. For the first nine months of the year, margins were $16.7 \%$ in 2001 and $20.1 \%$ in 2000 . The lower sales level in the third quarter 2001 versus the third quarter 2000 reduced the variable margin contribution by $\$ 13.2$ million. The lower production levels coupled with the related increase in unabsorbed manufacturing costs and the inventory reduction were the other main factors for the lower margins in the quarter and for the year thus far. The negative currency effect also impacted the Metal Systems Group's margins. The mix effect was unfavorable during the third quarter in part due to the $\$ 1.6$ million sale of beryllium containing input material with no margin.

Total SG\&A and Other-net expenses were $\$ 4.2$ million lower in the third quarter 2001 than in the third quarter 2000 while expenses for the first nine months of 2001 were $\$ 4.8$ million lower than the comparable period in 2000. Cost reduction efforts within TMI and Alloy in response to the declining sales volumes as well as a lower incentive compensation expense in 2001 were responsible for the improvement. Sales commissions are also lower in 2001. Severance and other one-time closure costs totaled $\$ 0.6$ million in the third quarter 2001.

The Metal Systems Group lost $\$ 9.4$ million in the third quarter 2001 compared to a profit of $\$ 3.6$ million in the third quarter 2000. For the first nine months of the year, the group lost $\$ 4.4$ million in 2001 and earned $\$ 5.8$ million in 2000, a difference of $\$ 10.2$ million between periods.

## MICROELECTRONICS GROUP

|  | THIRD QUARTER |  | FIRST NINE MONTHS |  |
| :---: | :---: | :---: | :---: | :---: |
| (Millions) | 2001 | 2000 | 2001 | 2000 |
| Sales. | \$41.7 | \$48.5 | \$130.9 | \$131.9 |
| Operating Profit | 0.2 | 3.1 | 3.5 | 7.8 |

After growing in the first half of 2001 over the first half of 2000, sales from the Microelectronics Group (MEG) declined $\$ 6.8$ million, or $14.1 \%$, in the third quarter 2001. Operating profit also declined from $\$ 3.1$ million in the third quarter 2000 to $\$ 0.2$ million in the third quarter 2001. While year-to-date sales are only $\$ 1.0$ million behind the 2000 level, operating profit in 2001 is $\$ 4.3$ million lower than last year. The MEG consists of Williams Advanced Materials Inc. (WAM) and Electronic Products. The following chart highlights business unit sales as a percent of the total Microelectronics Group sales:

|  | THIRD QUARTER |  | FIRST NINE MONTHS |  |
| :---: | :---: | :---: | :---: | :---: |
|  | 2001 | 2000 | 2001 | 2000 |
| Percent of Segment Sales |  |  |  |  |
| WAM. | 81.3\% | 77.5\% | 77.9\% | 76.3\% |
| Electronic Products. | 18.7 | 22.5 | 22.1 | 23.7 |

Revenues from WAM declined $9.8 \%$ in the third quarter 2001 from the third quarter 2000 while third quarter 2001 year-to-date revenues grew by $1.3 \%$. WAM manufactures physical vapor deposition targets, specialty alloys and packaging materials, including frame lid assemblies, bonding wire and solder preforms. The majority of these products contain precious metals and the comparison of revenues between periods can be affected by the cost and the mix of precious metals sold. The value added, which is sales less the cost of precious metals sold, actually increased by $5.5 \%$ in the third quarter and $12.8 \%$ for the first nine months compared to the same periods in 2000. While WAM experienced softening in orders from the wireless and photonics sectors of the microelectronic market during the third quarter 2001, the growth in other applications for targets, including DVD (digital video disk) and GMR (giant magnetic resistive) materials, has allowed WAM to increase its margins and profits. Frame lid assembly (FLA) sales and value added increased in the third quarter 2001 as a result of the acquisition of additional assets used in manufacturing FLA's from a competitor who withdrew from the market in the second quarter 2001. Specialty alloy volumes declined slightly in the third quarter 2001 from the third quarter 2000 as a result of the softening in the electronics market. WAM continued to re-invest in its business and now has manufacturing operations in four domestic and two foreign locations.

Sales by Electronic Products were $28.8 \%$ lower in the third quarter 2001 and $7.5 \%$ lower in the first nine months of 2001 versus the comparable periods in 2000. Beryllia ceramics, the largest product line within this business, was significantly affected by the telecommunications slow down, as sales of these products were off $44.2 \%$ in the third quarter 2001 from the year ago period. Beryllia ceramics are sold into a mature market with a limited customer base. Sales of thick film circuits, which had doubled in the first half of this year over the 2000 level, were essentially flat in the third quarter 2001 compared to the third quarter 2000. Direct bond copper and powder metal product sales were also slightly lower in the current year compared to last year.

Gross margin on MEG sales was $12.3 \%$ in the third quarter 2001 and $16.8 \%$ in the third quarter 2000. For the first nine months of the year, the gross margin was $14.9 \%$ in 2001 and $17.6 \%$ in 2000 . The variable margin contribution was $\$ 2.1$ million lower in the third quarter 2001 as a result of the reduced sales volumes.

Unfavorable inventory adjustments of $\$ 0.8$ million were recorded against gross margins in the third quarter 2001 due to obsolescence and other valuation issues.

Total SG\&A and Net-other expenses declined $\$ 0.2$ million in the third quarter 2001 from the third quarter 2000. Expenses for the first three quarters of 2001 were $\$ 0.6$ million higher than the first three quarters of 2000 . Selling expenses were higher in the quarter and for the year in order to support the increased WAM activities while administrative and incentive compensation expenses declined. Severance costs totaled $\$ 0.2$ million in the third quarter 2001. Precious metal financing fees were $\$ 0.3$ million lower in the third quarter 2001 and $\$ 0.6$ million lower in the first three quarters of 2001 compared to the same periods last year. The savings resulted from reduced quantities of metal on hand and lower financing rates.

Operating profit for the MEG was $\$ 0.2$ million in the third quarter 2001, a $\$ 2.9$ million decline from the third quarter 2000. Year-to-date operating profit was $\$ 3.5$ million in 2001 and $\$ 7.8$ million in 2000 . Year-to-date operating profit as a percent of sales was $2.9 \%$ in 2001 and $5.9 \%$ in 2000.

## LEGAL PROCEEDINGS

One of the Company's subsidiaries, Brush Wellman Inc., is a defendant in proceedings in various state and federal courts brought by plaintiffs alleging that they have contracted chronic beryllium disease ("CBD") or related ailments as a result of exposure to beryllium. Plaintiffs in CBD cases seek recovery under theories of intentional tort and various other legal theories and seek compensatory and punitive damages, in many cases of an unspecified sum. Spouses, if any, claim loss of consortium.

The following table summarizes the activity associated with CBD cases:


Additional CBD claims may arise. Management believes it has substantial defenses in these cases and intends to contest the suits vigorously. Employee cases, in which plaintiffs have a high burden of proof, have historically involved relatively small losses to the Company. Third party plaintiffs (typically employees of Brush Wellman's customers) face a lower burden of proof than do employees or former employees, but these cases are generally covered by insurance. In class actions, plaintiffs have historically encountered difficulty in obtaining class certification. The Company recorded a reserve for CBD litigation of $\$ 11.8$ million at September 28, 2001 and $\$ 9.1$ million at December 31, 2000. The Company also recorded a receivable of $\$ 5.0$ million at September 28, 2001 and $\$ 4.7$ million at December 31, 2000 from its insurance carriers as recoveries for insured claims.

Although it is not possible to predict the outcome of the litigation pending against the Company and its subsidiaries, the Company provides for costs related to these matters when a loss is probable and the amount is reasonably estimable. Litigation is subject to many uncertainties, and it is possible that some of these actions could be decided unfavorably in amounts exceeding the Company's reserves. An unfavorable outcome or settlement of a pending CBD case or additional adverse media coverage could encourage the commencement of additional similar litigation. The Company is unable to estimate its potential exposure to unasserted claims.

While the Company is unable to predict the outcome of the current or future CBD proceedings, based upon currently known facts and assuming collectibility of insurance, the Company does not believe that resolution of these proceedings will have a material adverse effect on the financial condition or the cash flow of the Company.

However, the Company's results of operations could be materially affected by unfavorable results in one or more of these cases.

Standards for exposure to beryllium are under review by governmental agencies, including the United States Occupational Safety and Health Administration, and by private standard setting organizations. One result of these reviews might be more stringent worker safety standards. More stringent standards, as well as other factors such as the adoption of beryllium disease compensation programs and publicity related to these reviews may also affect buying decisions by the users of beryllium containing products. If the standards are made more stringent or the Company's customers decide to reduce their use of beryllium containing products, the Company's operating results, liquidity and capital resources could be materially adversely affected. The extent of the adverse effect would depend on the nature and extent of the changes to the standards, the cost and ability to meet the new standards, the extent of any reduction in customer use and other factors that cannot be estimated.

## FINANCIAL POSITION

While the Company had a $\$ 0.3$ million net loss for the first three quarters of 2001, cash flow from operations was $\$ 17.0$ million during the period. The difference was primarily a result of the effects of depreciation and changes in working capital. Cash balances were $\$ 4.5$ million at the end of the third quarter 2001, an increase of $\$ 0.2$ million from December 31, 2000.

Accounts receivable declined $\$ 21.0$ million since the beginning of the current year. The lower sales volume in the current year is responsible for this reduction. The days sales outstanding increased by approximately four days since the fourth quarter 2000, but it did improve slightly in the third quarter 2001 over the second quarter 2001.

Inventories increased $\$ 3.3$ million during the first nine months of 2001. However, inventories declined $\$ 10.7$ million during the third quarter 2001 as a result of lower production volumes and plant shutdowns. The majority of the decrease in inventories in the third quarter was in the Metal Systems Group and Alloy Products in particular. Alloy inventory pounds declined $14.9 \%$ during the first three quarters of 2001, with the majority of the decrease coming from Elmore's work-in-process inventories. Scrap inventories at Elmore were also reduced significantly during the first three quarters of 2001. Inventory turns were unchanged from the second quarter, indicating that the inventory reduction in the third quarter was in line with the decreased sales volumes. Turns have slowed, however, since the fourth quarter 2000.

Capital expenditures were $\$ 20.9$ million for the first three quarters of 2001 . The Company slowed down the spending rate in the third quarter as capital expenditures totaled $\$ 15.8$ million in the first half of the year and only $\$ 5.1$ million in the third quarter. Approximately $55 \%$ of the year-to-date expenditures support the Metal Systems Group. Major projects for this Group include bulk product annealing equipment in Elmore, strip product annealing and pickling equipment in the Reading facility and precious metal plating equipment at TMI. Major capital projects within the MEG include a capacity expansion at the Company's thick film circuit manufacturing facility in Oceanside, CA. and the acquisition of the FLA manufacturing assets by WAM. The Company also purchased the land and mineral rights that were previously leased by its mining operations in Utah and land adjacent to its Utah milling facility for $\$ 1.3$ million. The purchased mineral rights cover approximately $95 \%$ of the Company's proven beryllium reserves.

Accounts payable and other liabilities and accrued items were a combined $\$ 17.6$ million lower at the end of the third quarter 2001 than at the beginning of the year as a result of reduced business volumes in the current year and payment of the accrued incentive compensation for 2000 in early 2001. Other long-term liabilities grew $\$ 6.3$ million as a result of changes to the legal liability reserves and changes in the carrying value of various derivative financial instruments.

Total balance sheet debt stood at $\$ 77.3$ million at the end of the third quarter, an increase of $\$ 8.5$ million since year-end 2000. The increase in debt occurred in the first half of the year as, even with the slow down in business and the operating loss in the third quarter, total debt was reduced by $\$ 6.5$ million from the end of the second quarter 2001. For the year, short-term debt increased $\$ 7.6$ million and long-term debt increased $\$ 0.9$ million. Short-term debt includes $\$ 17.7$ million of foreign currency denominated loans and $\$ 7.1$ million of a precious metal denominated facility. The increase in long-term debt was used to finance the majority of the Utah land purchase. The Company received a waiver from its bank group for certain covenants contained in its
revolving credit agreement and a synthetic lease obligation effective as of September 28, 2001. As part of that waiver, the banks took a security interest in the Company's domestic assets. The Company and its bank group agreed to discuss amending these agreements during the fourth quarter 2001. It is possible that, if amended, the agreements will eliminate, revise or add various covenants.

Dividends paid totaled $\$ 6.0$ million in the first nine months of 2001. Subsequent to the dividend payment in July, the Company announced the suspension of the normal $\$ 0.12$ per share quarterly dividend. The dividend was suspended in order to improve the Company's future cash and debt positions in light of the current operating loss and market conditions. The dividend payments were typically $\$ 2.0$ million per quarter.

The Company received $\$ 1.8$ million of cash for the purchase of common stock under stock option plans during the first three quarters of 2001. All of this cash was received in the first half of the year.

Cash flow from operations was $\$ 22.7$ million in the first nine months of 2000. Accounts receivable grew $\$ 21.8$ million during that time frame as a result of the record sales volumes and an increase in the days sales outstanding. Inventories decreased by $\$ 2.1$ million as the Company entered into an off balance sheet agreement to finance $\$ 8.3$ million of its copper-based inventory. Capital expenditures were $\$ 13.3$ million during the first three quarters of 2000 . The Company paid three quarterly dividends at $\$ 0.12$ per share totaling $\$ 5.9$ million. Total balance sheet debt declined $\$ 1.9$ million during the first nine months of 2000.

Funds generated by operations plus the available borrowing capacity are believed to be adequate to support operating requirements, capital expenditure requirements and remediation projects. Excess cash, if any, is invested in money market or other high quality investments.

## MARKET RISK DISCLOSURE

For information regarding the Company's market risks, refer to page 21 of the annual report to shareholders for the year ended December 31, 2000.

## OUTLOOK

Due to the degree of softening in the Company's major markets and the suddenness with which the global economic conditions affected the Company's sales, it is currently difficult to project business levels with a high degree of reliability. Major customers and end-use demand generators for the Company's products have indicated that their forecasts are changing rapidly and that they do not have much visibility into their future requirements. The Company's current outlook, therefore, does not call for any significant improvement in sales volumes in the near term. While the Company remains confident in the long-term potential of its various markets, it is unable to project when those markets and the over-all economy will improve. Sales in the fourth quarter 2001 may be lower than in the third quarter 2001 at least in part due to the fourth quarter having fewer shipping days than the third quarter.

Given the reduced sales volumes, the Company has and will continue to adjust its cost structure to improve its profitability. During the first nine months of 2001, the Company reduced its workforce by approximately $13 \%$. More reductions are anticipated to occur in the fourth quarter. Plant shutdowns, reduced work weeks and spending control and efficiency programs are being used to lower the Company's breakeven point. In addition, the Company has and will continue to implement plans to improve its cash flows. The rate of spending on capital programs has been slowed down and it is anticipated that capital expenditures in 2002 will be lower than in 2001. As previously noted, inventories were reduced in the third quarter and the quarterly dividend has been suspended. The Company will continue to evaluate its investment options in order to generate the optimal return on its working and fixed capital investments. The Company believes that a large portion of the recent changes in its cost structure are of a permanent nature and therefore will allow for a more rapid growth in profitability once its markets improve.

## PART II OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

The Company and its subsidiaries are subject, from time to time, to a variety of civil and administrative proceedings arising out of their normal operations, including, without limitation, product liability claims, health, safety and environmental claims and employment-related actions. Among such proceedings are the cases described below.

## CBD CLAIMS

There are claims pending in various state and federal courts against Brush Wellman, one of the Company's subsidiaries, by its employees, former employees or surviving spouses and third party individuals alleging that they contracted, or have been placed at risk of contracting, chronic beryllium disease ("CBD") or related ailments as a result of exposure to beryllium. Plaintiffs in CBD cases seek recovery under theories of intentional tort and various other legal theories and seek compensatory and punitive damages, in many cases of an unspecified sum. Spouses, if any, claim loss of consortium.

During the third quarter of 2001, the number of CBD cases grew from 79 cases (involving 211 plaintiffs) as of June 29, 2001 to 80 cases (involving 208 plaintiffs), as of September 28, 2001. During the third quarter, eight cases involving fourteen plaintiffs were dismissed. In one additional case, one plaintiff and his spouse voluntarily dismissed their claims, but the case remains pending with other plaintiffs.

The 80 pending CBD cases fall into three categories: 45 "employee cases" involving an aggregate of 46 Brush Wellman employees, former employees or surviving spouses (in 27 of these cases, a spouse has also filed claims as part of his or her spouse's case); 32 cases involving third party individual plaintiffs, with 67 individuals (and 44 spouses who have filed claims as part of their spouse's case, and ten children who have filed claims as part of their parent's case); and three purported class actions involving 13 individuals (and one spouse who has filed a claim as part of her spouse's case). Employee cases, in which plaintiffs have a high burden of proof, have historically involved relatively small losses to the Company. Third party plaintiffs (typically employees of our customers) face a lower burden of proof than do employees or former employees, but these cases are generally covered by insurance, at least partially.

In the three purported class actions that are pending against Brush Wellman, the named plaintiffs allege that past exposure to beryllium has increased their risk of contracting CBD, though most of them do not claim to have actually contracted it. They seek medical monitoring funds to be used to detect medical problems that they believe may develop as a result of their exposure and, in some cases, also seek compensatory and punitive damages.

One of the three purported class actions pending against Brush Wellman was brought by named plaintiffs on behalf of tradesmen who worked in one of Brush Wellman's facilities as employees of independent contractors. The two others were brought on behalf of current and former employees of Brush Wellman's present and former customers and vendors.

## OTHER CLAIMS

Brush Wellman's Egbert subsidiary has been named as a defendant in a number of lawsuits alleging asbestos-induced illness, arising out of the conduct of a friction materials business whose operating assets Egbert sold in 1986. In each of the pending cases, Egbert is one of a large number of defendants named in the respective complaints. Egbert is a party to an agreement with the predecessor owner of its operating assets, Pneumo Abex Corporation (formerly Abex Corporation), and five insurers, regarding the handling of these cases. Under the agreement, the insurers share some expenses of defense, and Egbert, Pneumo Abex Corporation and the insurers share payment of settlements and/or judgments. In each of the pending cases, both expenses of defense and payment of settlements and/or judgments are subject to a limited separate reimbursement agreement under which a successor owner of the business is obligated. A number of cases of this type have been disposed of to date,
some by voluntary dismissal, others by summary judgment, one by jury verdict of no liability, and still others upon payment of nominal amounts in settlement. There are at present 23 asbestos cases pending.

## CLAIMS CONCLUDED SINCE THE END OF SECOND QUARTER 2001

As previously reported in the Form 10-Q for the second quarter of 2001, a Consent Decree related to alleged violations of the Pima County Air Code was pending between Brush Wellman and the Pima County Air Quality Control District. On August 21, 2001, Brush Wellman and the District filed that Consent Decree and an accompanying Settlement Agreement in Arizona Superior Court. Under the Decree and the Agreement, Brush Wellman paid a civil penalty of $\$ 145,000$, and the matter was dismissed on August 27, 2001.

## ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

> (10) Second Amendment to the Deferred Compensation Plan for Non-Employee Directors (as amended through September 11, 2001).
> (11) Statement re computation of per share earnings (filed as Exhibit 11 to Part $I$ of this report).
(b) Reports on Form 8-K

Brush Engineered Materials Inc. filed a report on Form 8-K on August 28, 2001 that included a copy of a press release revising sales forecasts for the remainder of the year.

Brush Engineered Materials Inc. filed a report on Form 8-K on September 12, 2001 that included a copy of a press release suspending future dividend payments and revising forecasts for the remainder of the year.

## SIGNATURES

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.

BRUSH ENGINEERED MATERIALS INC.

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/s/ John D. Grampa
John D. Grampa
Vice President Finance
and Chief Financial Officer
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## MEMORANDUM

## BRUSH ENGINEERED MATERIALS INC.

## DEFERRED COMPENSATION PLAN FOR NONEMPLOYEE DIRECTORS

 (AS AMENDED THROUGH SEPTEMBER 11, 2001)This Memorandum relates to the Common Shares of Brush Engineered Materials Inc that have been reserved for sale under the plan named above. Company may supplement this memorandum from time to time.

- The purpose of this Memorandum is to summarize certain features of the Plan. You should refer to the plans if you have additional questions. If there is an inconsistency between the information in this Memorandum and the Plan, the Plan will govern.
- This Memorandum supersedes in its entirety, and takes the place of, the Memoranda dated June 29, 1992 and September 11, 1998.

The Securities and Exchange Commission wants you to know that:

- This document constitutes part of a prospectus covering securities that have been registered under the Securities Act of 1933.
- Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete.

Any representation to the contrary is a criminal offense.

The date of this Memorandum is October 24, 2001.
PAGE
GENERAL ..... 1
DESCRIPTION OF PLAN .....  1
Purpose and Adoption. .....  1
Operation of Plan ..... 1
Election to Participate .....  2
Conversion from the Directors' Retirement Plan.......................... 2
Investment of Trust Accounts3
Distribution of Company Accounts. ..... 3
Special Distribution of Company Accounts .....  4
Change in Control .....  4
Consequence of Company's Insolvency. .....  5
Trust Assets Subject to Claims of Company's Creditors;
Unfunded and Unsecured Nature of Company's Obligations........... 5
Voting of Common Shares Held in Trust......................................
Designation of Beneficiaries.................................................. 6
Payment or Withholding of Taxes................................................. 6Assignment of Nonemployee Director's Rights
or Beneficial Interest under Plan.......................................... 6
No Right to Continued Service. ..... 7
Nonqualified Status of Plan ..... 7
Administration of Plan. ..... 7
Amendment and Termination of Plan and Trust ..... 7
RESALES OF COMMON SHARES .....  8
TAX CONSEQUENCES. ..... 8
DESCRIPTION OF SECURITIES .....  8
INCORPORATION OF DOCUMENTS BY REFERENCE. ..... 10
ADDITIONAL INFORMATION ..... 11

## GENERAL

This Memorandum does not constitute an offer to sell or a solicitation of an offer to buy any securities other than the registered securities to which it relates or an offer to sell or a solicitation of an offer to buy any securities in any jurisdiction to any person to whom it is unlawful to make such an offer or solicitation.

Under no circumstances shall the delivery of this Memorandum or any sale made hereunder create any implication that there has been no change in the affairs of Brush Engineered Materials Inc. or in any of the information included herein or in any supplement hereto or in any document incorporated herein by reference since the date hereof or thereof.

## DESCRIPTION OF PLAN

## PURPOSE AND ADOPTION

The purpose of the Plan is to help solidify the common interest of directors and shareholders in enhancing the value of the Brush Engineered Materials Inc. Common Shares. The Plan was originally adopted by the Board of Directors of Brush Engineered Materials Inc. on December 17, 1991, and was approved by the shareholders of the Company on April 28, 1992.

On December 2, 1997, the Board amended the Plan to:

- Effect the transfer of accrued benefits from the Brush Wellman Inc. Directors' Retirement Plan As Amended January 26, 1993 to the Plan.
- Make deferral of fees available immediately to any new Nonemployee Director who came on the Board during the first half of the calendar year.
- Specify that Nonemployee Directors may not transfer existing account balances into or out of the Brush Stock fund.

On September 11, 2001, the Board amended the Plan to:

- Permit Directors who are age 55 or older to transfer investment funds from the Brush Stock Fund to one of the other funds and vice versa.
- Add new investment choices.
- Authorize special distributions at a discount.


## OPERATION OF PLAN

The Plan is designed to provide any member of the Board who is not an employee of Brush Engineered Materials Inc. with the opportunity to defer receipt (and therefore recognition as income for federal income tax purposes) of all or any portion of his compensation for services as a Nonemployee Director. (See "Intended Tax Effect of Plan Participation" below.) The Plan provides for this deferral by giving a Nonemployee Director the right to elect to reduce his current compensation. (See "Election to Participate" below.)

- credit the amount of the reduction to a Trust Account in the name of the Nonemployee Director on the books of the Company and
- contribute an amount equal to the amount of the reduction to a Trust maintained by National City Bank N.A., a Trustee, which will establish a corresponding Trust Account in the name of the Nonemployee Director under the Trust.

The Plan further provides that any compensation that was previously deferred pursuant to preexisting arrangements between a Nonemployee Director and the Company may also be transferred to the Trust. The Plan also provides for the transfer of accrued benefits from the Directors' Retirement Plan (See "Conversion from the Directors' Retirement Plan" below). The balance of a Nonemployee Director's Company Account will be adjusted from time to time to reflect income, earnings, losses and expenses credited or charged to his Trust Account.

At the time of distribution, the amount payable to a Nonemployee Director is based on the value of his Company Account. (See "Distribution of Company Accounts" and "Special Distribution of Company Accounts" below.) The Company's obligation to make payment to a Nonemployee Director will be satisfied from the Trust if the Company is not insolvent (as defined below) at the time. (See "Consequences of Company's Insolvency" below.)

## ELECTION TO PARTICIPATE

Any Nonemployee Director may participate in the Plan during any fiscal year by electing to defer receipt of all or a portion of his annual retainer, meeting fees and any other compensation that may be payable to him by the Company for his services as a Nonemployee Director. The election must be in writing on the form prescribed by the Company. It must be filed with the Administrative Committee appointed by the Board to administer the Plan prior to the beginning of any fiscal year during which a Nonemployee Director wishes to participate in the Plan. For example, a Nonemployee Director must file his election on or before December 31, 2001 if he wishes to participate in the Plan during 2002.

If a person becomes a Nonemployee Director for the first time after January 1 of any calendar year, he may file an election to participate in the Plan for that year if he files within 30 days after he becomes a Nonemployee Director during that year. His election will apply only to compensation for services rendered as a Nonemployee Director after the date on which it is filed. Once an election is made, it is irrevocable with respect to compensation for services rendered as a Nonemployee Director during the fiscal year to which it relates.

## CONVERSION FROM THE DIRECTORS' RETIREMENT PLAN

Not later than December 31, 1997, each Nonemployee Director was provided the opportunity to make an election to credit the present value as of December 31, 1997 of his vested benefit under the Directors' Retirement Plan (which was terminated as of December 31, 1997) to the Nonemployee Directors' Company Account. Following the filing of the written election with
the Committee, the Company transferred to the Trustee to be held in the Trust for the account of such Nonemployee Director the cash funds equal to the amount which each such Nonemployee Director elected to be converted from the Directors' Retirement Plan. Payment will be made as described below under "Distribution of Company Accounts." In no event will a Nonemployee Director be entitled to payment prior to termination of service as a Director.

## INVESTMENT OF TRUST ACCOUNTS

The accounts credited to a Nonemployee Director's Trust Account will be invested by the Trustee as directed by the Nonemployee Director in his written election to participate in the Plan. The authorized investment choices are as follows:

- Brush Common Shares Fund
- In accordance with the Investment Policy
- Templeton Foreign Fund
- Vanguard Asset Allocation Fund
- Vanguard Index Trust 500 Portfolio

A brief description of these funds and a table setting forth financial data of the past 3 years with respect to each of the investment funds is attached as APPENDIX A.

A Nonemployee Director may direct that the assets of his Trust Account be invested in part Common Shares and in part in any other authorized investment or investments in increments of five percent. A Nonemployee Director may change his election from time to time with respect to future additions to the Nonemployee Director Company Account, but may not change such election with respect to amounts previously credited at any time, except that a Director who is 55 years of age or older may change his or her election. [The form of election prescribed by the Committee provides that the election is irrevocable for the fiscal year to which it relates.] Any earnings with respect to the assets of a Nonemployee Director's Trust Account will be credited thereto and invested from time to time by the Trustee in accordance with the Nonemployee Director's most recent investment election.

If a Nonemployee Director elects to have the assets of his Trust Account invested by the Trustee in Common Shares, the Plan provides that the Trustee may purchase the Common Shares on the open market or from the Company. However, open market shares have also been used in the past and the Company intends to continue that practice. If this practice should be changed in the future, the Trustee will not pay more for Common Shares purchased from the Company than it would have paid on the open market.

## DISTRIBUTION OF COMPANY ACCOUNTS

Except in the case of a Special Distribution (described below), the amounts credited to a Nonemployee Director's Company Account will be distributed to him in either a lump sum or not more than 10 annual installments, as directed by the Nonemployee Director in
his initial election to participate in the Plan and at the time his or her vested benefits were converted from the Directors' Retirement Plan, within 10 days after the earliest to occur of

- the date on which the Nonemployee Director attains the age of 70,
- the date on which the Nonemployee Director ceases to be a member of the Board or
- the date on which a change in control (as defined below) of the Company occurs.

A Nonemployee Director cannot later change his distribution election. However, if the amount credited to any Nonemployee Director's Company Account is less than one year's retainer, the distribution will be in a lump sum on the date of termination. Also, if any Nonemployee Director electing to credit amounts to such Nonemployee Director's Company Account upon termination of the Director's Retirement Plan, ceases to be a Director within one year after signing such election other than by reason of death, disability or failure to be re-elected as a Nonemployee Director, the applicable portion of the distribution will be a lump sum.

If the Company is not insolvent at the time of any distribution, the distribution will be made from the Trust and charged to the Nonemployee Director's Trust Account. (See "Consequences of Company's Insolvency" below.) All distributions (whether from the Trust or directly from the Company) will be charged to the Nonemployee Director's Company Account. To the extent that the amounts credited to a Nonemployee Director's Company Account are invested in Common Shares at the time of distribution, the Common Shares will be distributed in kind. If a Nonemployee Director elects to receive a distribution in annual installments, the amount of each installment payment will be calculated by dividing the amount credited to his Company Account at the time of the payment (as determined by the Committee) by the number of remaining installments, including the then-current installment.

## SPECIAL DISTRIBUTION OF COMPANY ACCOUNTS

A Nonemployee Director may elect to receive a distribution of part or all of his or her Company Account in one or more distribution if (and only if) the amount in the Nonemployee Director's Company Account is reduced by $10 \%$.

A Nonemployee Director may elect to receive such special distribution in cash or in Common Shares. The special distribution will be made within 30 days after the election is submitted to the Committee. The remaining $10 \%$ of the portion of the Director's Company Account subject to such distribution shall be forfeited to Brush Engineered Materials Inc. A Nonemployee Director who is currently serving as a Director and elects a special distribution must immediately terminate his or her deferrals under the Plan for the balance of the year in which the election is submitted and for the following 2 years.

## CHANGE IN CONTROL

The Plan defines the term "change in control" to mean the occurrence of any of the following events:
(a) The Board at any time shall fail to include a majority of directors who are either "Original Directors" or "Approved Directors". An Original Director is a director who is serving on January 1, 1992. An Approved Director is a director who, after such date, is elected, or is nominated for election by the shareholders, by a vote of at least two-thirds of the Original Directors and the previously elected Approved Directors, if any;
(b) any person (as the term "person") is defined in Section 1701.01(G) of the Ohio Revised Code) shall have made a "control share acquisition" (as the term "control share acquisition" is defined in Section 17601.01(Z) of the Ohio Revised Code) of the Common Shares without having first complied with Section 1701.831 of the Ohio Revised Code (dealing with control share acquisitions); or
(c) The Board shall at any time determine in the good faith exercise of its judgment that (i) any particular actual or proposed accumulation of the Common Shares, tender offer for the Common Shares, merger, consolidation, sale of assets, proxy contest, or other transaction or event or series of transactions or events will, or is likely to, if carried out, result in a change in control falling within (a) or (b) above and (ii) it is in the best interests of the Company and its shareholders, and will serve the intended purposes of the Plan and the Trust, for distributions of Company Accounts to commence immediately in accordance with the Plan.

## CONSEQUENCE OF COMPANY'S INSOLVENCY

In the event that the Company becomes insolvent, the Board and the President of the Company will immediately notify the Trustee of that fact. After the Trustee has been so notified of the Company's insolvency or otherwise acquires knowledge thereof, the Trustee:

- will not make any payment or distribution to any Nonemployee Director or beneficiary and
- will transfer or deliver the assets of the Trust only as a court of competent jurisdiction may direct.

The Plan defines the term "insolvent" to mean that the Company is:

- subject to a pending voluntary or involuntary proceeding as a debtor under the United States Bankruptcy Code or
- unable to pay its debts as they mature.


## TRUST ASSETS SUBJECT TO CLAIMS OF COMPANY'S CREDITORS; UNFUNDED AND UNSECURED NATURE OF COMPANY'S OBLIGATIONS

All of the assets of the Trust, and any payment or distribution to be made by the Trustee to a Nonemployee Director, are subject to the claims of the Company's general creditors, including judgment creditors and bankruptcy creditors. The Company's obligation under the Plan is merely an unfunded and unsecured promise to pay money in the future. Neither a Nonemployee Director nor his beneficiaries, heirs, successors or assigns have any secured
interest in or claim against any of the assets of the Company or the Trust. The rights of Nonemployee Directors and their beneficiaries to the assets of the Trust are no greater than those of other unsecured creditors of the Company.

## VOTING OF COMMON SHARES HELD IN TRUST

All Common Shares credited to a Nonemployee Director's Trust Account will be voted by the Trustee in accordance with the Nonemployee Director's instructions. In the absence of any such instructions, the Trustee will vote the Common Shares credited to a Nonemployee Director's Trust Account in proportion to the votes of all other shareholders of the Company.

## DESIGNATION OF BENEFICIARIES

Each Nonemployee Director who elects to participate in the Plan may designate one or more beneficiaries to whom distributions will be made in the event that the Nonemployee Director dies before all distributions have been made to him. If a Nonemployee Director does not designate any beneficiaries or there is no designated beneficiary surviving at the time of the Nonemployee Director's death, the Nonemployee Director's sole beneficiary will automatically be his estate. Designations of beneficiaries must be made in writing and may be changed at any time by filing a new election with the Committee.

## PAYMENT OR WITHHOLDING OF TAXES

In the event that any taxes are required by law to be paid or withheld from any payments or distributions to be made by the Company or the Trustee pursuant to the Plan or the Trust, the Company or the Trustee, as the case may be, will deduct the amount of any such taxes from the payment or distribution and deliver to the appropriate taxing authority any amount so deducted.

## ASSIGNMENT OF NONEMPLOYEE DIRECTOR'S RIGHTS OR BENEFICIAL INTEREST UNDER PLAN

No right or interest of any Nonemployee Director or beneficiary (or any person claiming through or under a Nonemployee Director or beneficiary) in any benefit or payment under the Plan may be:

- assigned or transferred in any manner,
- subject to alienation, anticipation, encumbrance, pledge, sale or other legal process or
- liable in any manner for or subject to the debts or liabilities of the Nonemployee Director.

If any Nonemployee Director or other such person (other than the surviving spouse of a deceased Nonemployee Director) attempts to or does alienate, anticipate, assign, pledge, sell, transfer or otherwise encumber all or any part of his benefits under the Plan, or if by
reason of his bankruptcy or other circumstance any or all of his benefits under the Plan would devolve upon someone else or would otherwise not be enjoyed by him, the Committee may terminate his interest in all or any part of his benefits under the Plan to the extent that the Committee considers necessary or advisable in order to prevent or limit the effects of any such occurrence. Any such action by the Committee must be evidenced by a written "termination declaration", which must be filed with the records of the Committee, and the Committee must make reasonable efforts to deliver a copy to the Nonemployee Director or other such person whose interests are adversely affected thereby.

As long as any terminated participant is alive, any benefits affected by the termination declaration will be retained by the Trust and, at the discretion of the Committee, may be paid to or expended for the benefit of the terminated participant or his spouse, children or other persons who are in fact dependent upon him in whatever manner the Committee may deem appropriate. Upon the death of any terminated participant, all benefits that were withheld from him pursuant to a termination declaration and were not theretofore distributed at the discretion of the Committee will be distributed to his estate or his creditors, and if he has living descendants, the distribution will be made to those descendants PER STIRPES. All payments or distributions described in this paragraph will be made from the Trust if the Company is not insolvent at the time.

## NO RIGHT TO CONTINUED SERVICE

Nothing in the Plan will be construed as conferring upon any Nonemployee Director the right to continue to serve the Company as a member of the Board or otherwise.

## NONQUALIFIED STATUS OF PLAN

The Plan is not qualified under Section 401(a) of the Code and is not subject to the Employee Retirement Income Security Act of 1974.

## ADMINISTRATION OF PLAN

The Committee will consist of not less than three persons who (i) serve at the pleasure of the Board and may be dismissed at any time with or without cause and (ii) need not be members of the Board. The Committee will administer the Plan and resolve all questions of interpretation that may arise under the Plan. Any elections, directions, designations or other notices to be made or given by a Nonemployee Director pursuant to the Plan must be filed with the Committee. Except as discussed under "Assignment of Nonemployee Director's Rights or Beneficial Interest under Plan" above, the Committee has no discretion with respect to contributions or distributions pursuant to the Pan.

## AMENDMENT AND TERMINATION OF PLAN AND TRUST

The Company reserves the right to amend the Plan and the terms of the Trust or terminate the Plan at any time, except that no amendment or termination may affect the rights of Nonemployee Directors to:

- amounts previously credited to their Company Accounts or
- additional amounts credited thereto for earnings on the assets thereof following termination.

The Trust will remain in effect until its entire corpus has been distributed. The Plan will remain in effect until all amounts credited to Company Accounts have been distributed, in accordance with the Plan.

## RESALES OF COMMON SHARES

Nonemployee Directors who are "affiliates" of the Company may resell Common Stock acquired under the Plan in brokerage transactions on the New York Stock Exchange without registration under the Securities Act of 1933 under compliance with Rule 144 of the Securities and Exchange Commission, except that the one-year holding period requirement of Rule 144 will not apply. For this purpose, the term "affiliate" includes any Nonemployee Director who directly, or through one or more intermediaries, controls, or is controlled by, or is under common control with, the Company. Nonemployee Directors who are not "affiliates" may make resales in such brokerage transactions or otherwise without the need to comply with Rule 144.

## TAX CONSEQUENCES

The Plan is intended to be treated as an unfunded deferred compensation plan under the Internal Revenue Code of 1986 (the "Code"). It is the Company's intention that the amounts by which Nonemployee Directors elect to have their compensation reduced pursuant to the Plan will not be included in the gross income of the Nonemployee Directors or their beneficiaries until such time as distributions are made pursuant to the Plan. If at any time the Company determines that amounts attributable to either the Nonemployee Directors' of their compensation-reduction elections or their Company Accounts are includible in the gross income of the Nonemployee Directors or their beneficiaries prior to distribution pursuant to the Plan, all such amounts will immediately be paid or distributed to the Nonemployee Directors or their beneficiaries or estates, as the case may be; these payments or distributions will be made from the Trust if the Company is not insolvent at the time.

## BECAUSE THE TAX CONSEQUENCES TO A PARTICIPANT MAY VARY DEPENDING ON HIS INDIVIDUAL CIRCUMSTANCES, EACH PARTICIPANT SHOULD CONSULT HIS PERSONAL TAX ADVISOR REGARDING THE FEDERAL AND ANY STATE, LOCAL OR FOREIGN TAX CONSEQUENCES TO HIM.

## DESCRIPTION OF SECURITIES

Brush Engineered Materials Inc. has authority to issue up to $60,000,000$ shares of common stock and $5,000,000$ shares of serial preferred stock. Neither the common stock nor the preferred stock has par value. The board of directors may cause Brush Engineered Materials to issue shares of serial preferred stock in series with rights and privileges that may be superior to those of the holders of common stock. No serial preferred stock is outstanding.

Each share of common stock is entitled to one vote. Ohio law permits cumulative voting for the election of directors, if specified statutory procedures are followed. The board of
directors consists of two classes of three directors and one class of four directors. The shareholders elect each director to a three-year term.

All shares of common stock have an equal right to participate in dividends declared and, in the event of liquidation, in the net assets of Brush Engineered Materials Inc. Holders of shares of common stock have no preemptive rights to purchase presently authorized and unissued shares. The outstanding shares of common stock are, and the shares to be sold under the 1995 plan and the 1997 plan will be, when issued, fully paid and non-assessable.

If Brush Engineered Materials Inc. plans to engage in a transaction involving an owner of $10 \%$ or more (but less than $90 \%$ ) of its voting stock, that transaction must be approved by both of the following:

- Holders of a majority of Brush Engineered Materials Inc.'s voting stock; and
- Holders of a majority of Brush Engineered Materials Inc.'s disinterested shares (meaning the outstanding voting stock of Brush Engineered Materials Inc., excluding the shares owned by the party who owns $10 \%$ or more of the voting stock).

However, approval is not required if "fair price" criteria are satisfied or the transaction is approved by a majority of the "continuing directors" (as defined in Brush Engineered Materials Inc.'s articles of incorporation).

Among other things, the shareholder approval provision described above requires the second step of a "two-step" takeover to be approved by both a majority of Brush Engineered Materials Inc.'s outstanding voting power and a majority of the disinterested shares, unless either:

- The consideration offered for shares to be acquired in the second step is equal to, or greater than, that paid in the first step; or
- The transaction is approved by a majority of the continuing directors.

Brush Engineered Materials Inc.'s board of directors has adopted a defensive mechanism commonly referred to as a "poison pill." To do so, it adopted a rights agreement and declared a dividend of one preferred stock purchase right for each outstanding share of common stock. Each right entitles the shareholder to buy one one-hundredth of a share of Series A Serial Preferred Stock at an initial exercise price of $\$ 110$. The rights are not exercisable and will not be evidenced by separate right certificates until a specified time after any person or group acquires beneficial ownership of $20 \%$ or more (or announces a tender offer for $20 \%$ or more) of Brush Engineered Materials Inc.'s common stock.

After the rights become exercisable, if Brush Engineered Materials Inc. is a party to certain merger or business combination transactions or transfers $50 \%$ or more of its assets or earning power, or if the acquirer engages in certain self-dealing practices, or if (under certain circumstances) a person or group becomes the beneficial owner of $20 \%$ or more of Brush

Engineered Materials Inc.'s common stock, each right (except those held by the acquirer) will entitle its holder to purchase shares of common stock (or, under certain circumstances, the acquirer's common stock) worth twice the exercise price. Brush Engineered Materials Inc. can redeem the rights for one cent per right under some circumstances.

## INCORPORATION OF DOCUMENTS

## BY REFERENCE

The U.S. Securities and Exchange Commission or SEC allows Brush Engineered Materials Inc. to "incorporate by reference" the information filed with the SEC. This means:

- Incorporated documents are considered part of this Memorandum;
- Brush Engineered Materials Inc. can disclose important information to you by referring to those documents; and
- Information that Brush Engineered Materials Inc. files with the SEC will automatically update this Memorandum.

The following documents heretofore or hereafter filed by Brush Engineered Materials Inc. with the Commission are incorporated herein by reference:

- Annual Report on Form 10-K for the year ended December 31, 2000;
- Quarterly Reports on Form 10-Q for the quarters ended March 31, 2001 and June 29, 2001;
- Current Reports on Form 8-K, dated July 26, 2001, August 28, 2001 and September 12, 2001;
- The description of Brush Engineered Materials Inc.'s Common Shares contained in Brush Engineered Materials Inc.'s Registration Statement filed pursuant to Section 12 of the Exchange Act, including all amendments and reports filed for the purpose of updating that description;
- Rights Agreement dated May 10, 2000 between Brush Engineered Materials Inc. and National City Bank, N.A., as Rights Agreement (filed as Exhibit 4(a) to Current Report on Form 8-K filed on May 16, 2000; and
- All reports filed pursuant to Sections 13(a), 13(c), 14 and 15(d) of the Exchange Act prior to the filing of a post-effective amendment indicating that all of the securities offered under the Plan have been sold or deregistering all securities then remaining unsold thereunder.

Any statement contained in any document incorporated or deemed to be incorporated herein by reference shall be deemed to be modified or superseded for purposes of this Memorandum to the extent that a statement contained herein or in any other subsequently filed document that is also incorporated or deemed to be incorporated herein by reference modifies or
supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Memorandum.

## ADDITIONAL INFORMATION

Additional information about the Plan and the administrator may be obtained from, and copies of the following documents or reports will be furnished without charge upon oral or written request to, Michael C. Hasychak, Secretary and Treasurer, Brush Wellman Inc., 17876 St. Clair Avenue, Cleveland, Ohio 44110 (telephone number 216-486-4200):

- Documents or reports incorporated by reference into this Memorandum, excluding exhibits to such documents or reports unless such exhibits are specifically incorporated by reference into such documents or reports;
- Brush Engineered Materials Inc.'s annual report to shareholders for the latest fiscal year; and
- All reports, proxy statements and other communications distributed to Brush Engineered Materials Inc. shareholders.

All directors, officers and other key employees of Brush Engineered Materials Inc. and its subsidiaries who participate in the Plan will receive copies of all reports, proxy statements and other communications distributed to Brush Engineered Materials Inc.'s shareholders in general. Such materials will be delivered to participants not later than the time at which they are sent to Brush Engineered Materials Inc.'s shareholders.

## APPENDIX A

## INVESTMENT FUNDS

## Brush Common Stock Fund

The investment goal of this Fund is to invest in Common Shares of Brush Engineered Materials Inc. YOU SHOULD READ THE "DESCRIPTION OF SECURITIES"
INCLUDED IN THE MEMORANDUM, CAREFULLY IN ITS ENTIRETY. The Fund's annual rates of return for each of the last three years ending December 31 (and the period through September 30, 2001) were as follows:


## Investment Policy

The investment goal of this Fund is to invest in accordance with the Investment Policy set forth in Appendix B. There is no historical data available for investing in accordance with the Investment Policy.

## Templeton Foreign Fund

The investment goal of this Fund is long-term capital growth. The Fund tries to achieve its investment goal by a flexible policy of investing in the equity and debt securities of companies and governments outside the U.S. YOU SHOULD READ THE PROSPECTUS FOR THIS FUND, WHICH HAS BEEN PROVIDED TO YOU WITH THIS MEMORANDUM, CAREFULLY IN ITS ENTIRETY. The Fund's annual rates of return for each of the last three years ending December 31 (and the period through September 30, 2001) were as follows:





## Vanguard Asset Allocation Fund, Inc.

Vanguard Asset Allocation Fund, Inc. is an open-end diversified investment company that seeks to maximize total return (i.e., capital change plus income). The Fund invests in common stocks, bonds and money market instruments in proportions consistent with their expected returns and risks as evaluated by the Fund's adviser. YOU SHOULD READ THE PROSPECTUS FOR THIS FUND, WHICH HAS BEEN PROVIDED TO YOU WITH THIS MEMORANDUM, CAREFULLY IN ITS ENTIRETY. The Fund's annual rates of return for each of the last three years ending December 31 (and the period through September 30, 2001) were as follows:


## Vanguard Index Trust, 500 Portfolio

The Vanguard Index Trust, 500 Portfolio is a portfolio in an open-end investment company, which seeks to match, as closely as possible, the performance of the Standard \& Poor's 500 Composite Stock Price Index, which emphasizes stocks of large U.S. companies. YOU SHOULD READ THE PROSPECTUS FOR THIS FUND, WHICH HAS BEEN PROVIDED TO YOU WITH THIS MEMORANDUM, CAREFULLY IN ITS ENTIRETY. The Fund's annual rates of return for each of the last three years ending December 31 (and the period through September 30, 2001) were as follows:


Historical results of the various Funds do not necessarily indicate what future performance will be. Brush Engineered Materials Inc. cannot, and does not, guarantee the performance of any of the Funds and has no obligation to make up any losses suffered by participants.

Information about the Funds (other than the Brush Stock Fund) was derived from prospectuses and other reports provided by the investment companies in which they are invested, and Brush Engineered Materials Inc. makes no representation as to the accuracy of such information or the more detailed information set forth in such documents.

## Appendix B

## BRUSH ENGINEERED MATERIALS INC.

## INVESTMENT POLICY

## I PURPOSE

The purpose of this document is to state Brush Engineered Materials Inc.'s Investment Policy. The primary criteria for investments made under the Policy shall be preservation of principal and liquidity. The rate of return on investments while important shall not take precedence over safety of capital.

## II. POLICY

## A. ACCEPTABLE SECURITIES

1. With the exception of original issue discount securities such at T-Bills, federal agency securities, bankers acceptances and commercial paper only money market tax free, tax advantaged and taxable securities purchased and sold/put at par (100) are allowable portfolio holdings. Securities are not to be sold if a loss would be incurred. Investments which by nature fluctuate in price and do not have a year or less maturity or put at 100 are not acceptable. Examples of acceptable securities are Lower Floaters, unit priced demand adjustable tax exempt securities, put bonds, certificates of deposit, repurchase agreements, eurodollar time deposits and money market instruments.

## a. TAX EXEMPT ISSUES

Tax Free Variable Rate Demand Obligations and put bonds issued prior to 1986 should be given preference. Issues dated on or within three months before August 7, 1986 should be given extra scrutiny with regard to actual dated date as to insure federally tax free status.
2. Brush Engineered Materials Inc. receives an Ohio corporate franchise tax benefit for all federally tax exempt purchases. In addition, Arizona, Pennsylvania, Michigan and Rhode Island state and local tax exempt issues would generate an additional benefit in those respective states.

## B. INVESTMENT LIMITS AND LIQUIDITY REQUIREMENTS

1. A minimum of $30 \%$ of portfolio par value shall be invested in securities saleable with a 7 day or less settlement at price of par. No more than $20 \%$ may be invested in securities with actual or effective maturities between 6 months and 1 year.
2. Securities subject to alternative minimum tax are disallowed.
3. No more than $30 \%$ of the total market portfolio shall be invested in securities with the same entity supplying the underlying credit or same issuer except the federal government.
4. The total par value of each security shall be considered in determining each of the preceding II. B. Subsections 1 and 3 . Repurchase agreements and eurodollar time deposits shall not be aggregated in the total par value for Brush Engineered Materials cash management designated banks.

## C. CREDIT STANDARDS

Securities purchased should have a credit rating by Moodys of AA or the equivalent by Standard \& Poor's or alternatively:

1. The issue is backed by a credit enhancer of a bank rated AA or better and/or insurance company which provides for payment of principal and interest to cover a put and issuer default.
2. If the issue is unrated, have never applied, it must have an AA equivalent rating.
3. Commercial Paper must be rated $\mathrm{A} 1 / \mathrm{P} 1$.

## III. SAFEKEEPING

National City Bank will provide safe housing of all securities purchased for Brush Engineered Materials Inc. Exceptions to the safe housing arrangement shall be approved by the Treasury function.

## IV. GENERAL POLICY AND PROCEDURE

Any changes or exceptions to the policies and procedures as described in this document shall require written approval of the Treasurer of Brush Engineered Materials Inc.

## BRUSH ENGINEERED MATERIALS INC.

Dated: $\qquad$ By: $\qquad$

Its: $\qquad$
parameters established by said policy.
Dated: $\qquad$ By: $\qquad$

Its: $\qquad$
hereby acknowledges it has received and reviewed this investment policy and will act within the

## EXHIBIT 11

## BRUSH ENGINEERED MATERIALS INC. AND SUBSIDIARIES

COMPUTATION OF PER SHARE EARNINGS

|  | THIRD QUARTER ENDED |  | NINE MONTHS ENDED |  |
| :---: | :---: | :---: | :---: | :---: |
|  | $\begin{gathered} \text { SEP } 28 \\ 2001 \end{gathered}$ | $\begin{gathered} \text { SEP } 29 \\ 2000 \end{gathered}$ | $\begin{gathered} \text { SEP } 28 \\ 2001 \end{gathered}$ | $\begin{gathered} \text { SEP } 29 \\ 2000 \end{gathered}$ |
| Basic: |  |  |  |  |
| Average shares outstanding. | 16,548,410 | 16,315,523 | 16,508,784 | 16,248,733 |
| Net income. | \$ (7, 767,000) | \$ 4,084,000 | \$ $(286,000)$ | \$10,231,000 |
| Per share amount | \$ (0.47) | \$ 0.25 | \$ (0.02) | \$ 0.63 |
| Diluted: |  |  |  |  |
| Average shares outstanding. | 16,548,410 | 16,315,523 | 16,508,784 | 16,248,733 |
| Dilutive stock options based on the treasury stock method using average market price............................. | -- | 205,505 | -- | 143,702 |
| Totals. | 16,548,410 | 16,521,028 | 16,508,784 | 16,392,435 |
| Net income | \$ (7, 767,000) | \$ 4,084,000 | \$ $(286,000)$ | \$10,231,000 |
| Per share amount | \$ (0.47) | \$ 0.25 | \$ (0.02) | \$ 0.62 |

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