

TOOTSIE ROLL INDUSTRIES INC

Form 10-Q

May 10, 2018

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2018

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 1-1361

Tootsie Roll Industries, Inc.

(Exact Name of Registrant as Specified in its Charter)

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VIRGINIA 22-1318955  
(State of Incorporation) (I.R.S. Employer Identification No.)

7401 South Cicero Avenue, Chicago, Illinois 60629  
(Address of Principal Executive Offices) (Zip Code)

773-838-3400

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

Large accelerated filer

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date (March 31, 2018).

| Class                                     | Outstanding |
|-------------------------------------------|-------------|
| Common Stock, \$.69 4/9 par value         | 38,723,788  |
| Class B Common Stock, \$.69 4/9 par value | 25,637,487  |

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TOOTSIE ROLL INDUSTRIES, INC.

March 31, 2018

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This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. See “Forward-Looking Statements” under Part I — Item 2 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Quarterly Report on Form 10-Q.



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## PART I - FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## TOOTSIE ROLL INDUSTRIES, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(in thousands) (Unaudited)

|                                                                          | March 31,<br>2018 | December 31,<br>2017 | March 31,<br>2017 |
|--------------------------------------------------------------------------|-------------------|----------------------|-------------------|
| <b>ASSETS</b>                                                            |                   |                      |                   |
| <b>CURRENT ASSETS:</b>                                                   |                   |                      |                   |
| Cash & cash equivalents                                                  | \$ 49,867         | \$ 96,314            | \$ 78,555         |
| Restricted cash                                                          | 417               | 406                  | 389               |
| Investments                                                              | 60,321            | 41,606               | 67,002            |
| Trade accounts receivable, less allowances of \$1,914, \$1,921 & \$1,937 | 42,039            | 47,354               | 38,665            |
| Other receivables                                                        | 7,857             | 5,425                | 3,596             |
| Inventories:                                                             |                   |                      |                   |
| Finished goods & work-in-process                                         | 41,090            | 31,922               | 40,585            |
| Raw material & supplies                                                  | 26,904            | 22,905               | 27,196            |
| Income taxes receivable                                                  | 10,257            | 12,974               | -                 |
| Prepaid expenses                                                         | 9,077             | 12,014               | 4,022             |
| Total current assets                                                     | 247,829           | 270,920              | 260,010           |
| <b>PROPERTY, PLANT &amp; EQUIPMENT, at cost:</b>                         |                   |                      |                   |
| Land                                                                     | 22,011            | 21,962               | 22,138            |
| Buildings                                                                | 118,569           | 118,491              | 116,492           |
| Machinery & equipment                                                    | 381,805           | 381,665              | 370,430           |
| Construction in progress                                                 | 11,951            | 4,866                | 7,776             |
|                                                                          | 534,336           | 526,984              | 516,836           |
| Less-accumulated depreciation                                            | 352,597           | 348,012              | 336,074           |
| Net property, plant and equipment                                        | 181,739           | 178,972              | 180,762           |
| <b>OTHER ASSETS:</b>                                                     |                   |                      |                   |

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|                                     |            |            |            |
|-------------------------------------|------------|------------|------------|
| Goodwill                            | 73,237     | 73,237     | 73,237     |
| Trademarks                          | 175,024    | 175,024    | 175,024    |
| Investments                         | 195,911    | 190,510    | 195,312    |
| Split dollar officer life insurance | 26,042     | 26,042     | 26,042     |
| Prepaid expenses and other assets   | 14,731     | 15,817     | 344        |
| Deferred income taxes               | 457        | 424        | -          |
| Total other assets                  | 485,402    | 481,054    | 469,959    |
| Total assets                        | \$ 914,970 | \$ 930,946 | \$ 910,731 |

(The accompanying notes are an integral part of these statements.)

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(in thousands except per share data) (Unaudited)

|                                                                                                                       | March 31,<br>2018 | December 31,<br>2017 | March 31,<br>2017 |
|-----------------------------------------------------------------------------------------------------------------------|-------------------|----------------------|-------------------|
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                                                           |                   |                      |                   |
| <b>CURRENT LIABILITIES:</b>                                                                                           |                   |                      |                   |
| Accounts payable                                                                                                      | \$ 15,100         | \$ 11,928            | \$ 12,093         |
| Bank loans                                                                                                            | 425               | 440                  | 133               |
| Dividends payable                                                                                                     | 161               | 5,660                | 162               |
| Accrued liabilities                                                                                                   | 37,622            | 45,157               | 42,337            |
| Postretirement health care                                                                                            | 603               | 603                  | 513               |
| Income taxes payable                                                                                                  | -                 | -                    | 2,023             |
| Total current liabilities                                                                                             | 53,911            | 63,788               | 57,261            |
| <b>NONCURRENT LIABILITIES:</b>                                                                                        |                   |                      |                   |
| Deferred income taxes                                                                                                 | 41,431            | 41,457               | 44,330            |
| Bank loans                                                                                                            | -                 | -                    | 197               |
| Postretirement health care                                                                                            | 12,992            | 12,894               | 11,726            |
| Industrial development bonds                                                                                          | 7,500             | 7,500                | 7,500             |
| Liability for uncertain tax positions                                                                                 | 4,861             | 4,817                | 5,263             |
| Deferred compensation and other liabilities                                                                           | 67,815            | 66,686               | 77,655            |
| Total noncurrent liabilities                                                                                          | 134,599           | 133,354              | 146,671           |
| <b>TOOTSIE ROLL INDUSTRIES, INC. SHAREHOLDERS' EQUITY:</b>                                                            |                   |                      |                   |
| Common stock, \$.69-4/9 par value- 120,000 shares authorized;<br>38,724, 37,960 & 38,580, respectively, issued        | 26,891            | 26,361               | 26,792            |
| Class B common stock, \$.69-4/9 par value- 40,000 shares authorized;<br>25,637, 24,891 & 24,932, respectively, issued | 17,804            | 17,285               | 17,314            |
| Capital in excess of par value                                                                                        | 703,194           | 656,752              | 680,440           |
| Retained earnings                                                                                                     | 2,306             | 57,225               | 3,405             |
| Accumulated other comprehensive loss                                                                                  | (21,683)          | (21,791)             | (19,294)          |
| Treasury stock (at cost)- 88, 85 & 85 shares, respectively                                                            | (1,992)           | (1,992)              | (1,992)           |
| Total Tootsie Roll Industries, Inc. shareholders' equity                                                              | 726,520           | 733,840              | 706,665           |
| Noncontrolling interests                                                                                              | (60)              | (36)                 | 134               |
| Total equity                                                                                                          | 726,460           | 733,804              | 706,799           |
| Total liabilities and shareholders' equity                                                                            | \$ 914,970        | \$ 930,946           | \$ 910,731        |

(The accompanying notes are an integral part of these statements.)



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TOOTSIE ROLL INDUSTRIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF

EARNINGS AND RETAINED EARNINGS

(in thousands except per share amounts) (Unaudited)

|                                                                      | Quarter Ended     |                   |
|----------------------------------------------------------------------|-------------------|-------------------|
|                                                                      | March 31,<br>2018 | March 31,<br>2017 |
| Net product sales                                                    | \$ 100,859        | \$ 103,425        |
| Rental and royalty revenue                                           | 941               | 1,030             |
| Total revenue                                                        | 101,800           | 104,455           |
| Product cost of goods sold                                           | 65,834            | 65,538            |
| Rental and royalty cost                                              | 267               | 266               |
| Total costs                                                          | 66,101            | 65,804            |
| Product gross margin                                                 | 35,025            | 37,887            |
| Rental and royalty gross margin                                      | 674               | 764               |
| Total gross margin                                                   | 35,699            | 38,651            |
| Selling, marketing and administrative expenses                       | 25,857            | 26,725            |
| Earnings from operations                                             | 9,842             | 11,926            |
| Other income (loss), net                                             | 521               | 2,228             |
| Earnings before income taxes                                         | 10,363            | 14,154            |
| Provision for income taxes                                           | 2,262             | 4,143             |
| Net earnings                                                         | 8,101             | 10,011            |
| Less: Net earnings (loss) attributable to noncontrolling interests   | (24)              | (40)              |
| Net earnings attributable to Tootsie Roll Industries, Inc.           | \$ 8,125          | \$ 10,051         |
| Net earnings attributable to Tootsie Roll Industries, Inc. per share | \$ 0.13           | \$ 0.15           |
| Dividends per share *                                                | \$ 0.09           | \$ 0.09           |
| Average number of shares outstanding                                 | 64,434            | 65,474            |
| Retained earnings at beginning of period                             | \$ 57,225         | \$ 43,833         |
| Net earnings attributable to Tootsie Roll Industries, Inc.           | 8,125             | 10,051            |
| Adopted ASU's (See Note 1)                                           | 2,726             | -                 |
| Cash dividends                                                       | (5,621)           | (5,555)           |
| Stock dividends                                                      | (60,149)          | (44,924)          |
| Retained earnings at end of period                                   | \$ 2,306          | \$ 3,405          |

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\*Does not include 3% stock dividend to shareholders of record on 3/6/18 and 3/7/17.

(The accompanying notes are an integral part of these statements.)

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TOOTSIE ROLL INDUSTRIES, INC.

## CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE EARNINGS

(in thousands except per share amounts) (Unaudited)

|                                                                                 | Quarter Ended     |                   |
|---------------------------------------------------------------------------------|-------------------|-------------------|
|                                                                                 | March 31,<br>2018 | March 31,<br>2017 |
| Net earnings                                                                    | \$ 8,101          | \$ 10,011         |
| Other comprehensive income (loss), before tax:                                  |                   |                   |
| Foreign currency translation adjustments                                        | 1,612             | 2,100             |
| Pension and postretirement reclassification adjustments:                        |                   |                   |
| Unrealized gains (losses) for the period on postretirement and pension benefits | -                 | 266               |
| Less: reclassification adjustment for (gains) losses to net earnings            | (331)             | (365)             |
| Unrealized gains (losses) on postretirement and pension benefits                | (331)             | (99)              |
| Investments:                                                                    |                   |                   |
| Unrealized gains (losses) for the period on investments                         | (1,250)           | 230               |
| Less: reclassification adjustment for (gains) losses to net earnings            | -                 | -                 |
| Unrealized gains (losses) on investments                                        | (1,250)           | 230               |
| Derivatives:                                                                    |                   |                   |
| Unrealized gains (losses) for the period on derivatives                         | (1,472)           | (550)             |
| Less: reclassification adjustment for (gains) losses to net earnings            | 287               | (1,122)           |
| Unrealized gains (losses) on derivatives                                        | (1,185)           | (1,672)           |
| Total other comprehensive income (loss), before tax                             | (1,154)           | 559               |
| Income tax benefit (expense) related to items of other comprehensive income     | 669               | 393               |
| Total comprehensive earnings                                                    | 7,616             | 10,963            |
| Comprehensive earnings (loss) attributable to noncontrolling interests          | (24)              | (40)              |
| Total comprehensive earnings attributable to Tootsie Roll Industries, Inc.      | \$ 7,640          | \$ 11,003         |

(The accompanying notes are an integral part of these statements.)

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## TOOTSIE ROLL INDUSTRIES, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands) (Unaudited)

|                                                                                 | Quarter Ended     |                   |
|---------------------------------------------------------------------------------|-------------------|-------------------|
|                                                                                 | March 31,<br>2018 | March 31,<br>2017 |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                    |                   |                   |
| Net earnings                                                                    | \$ 8,101          | \$ 10,011         |
| Adjustments to reconcile net earnings to net cash used in operating activities: |                   |                   |
| Depreciation and amortization                                                   | 4,578             | 4,714             |
| Deferred income taxes                                                           | (415)             | (230)             |
| Amortization of marketable security premiums                                    | 456               | 593               |
| Changes in operating assets and liabilities:                                    |                   |                   |
| Accounts receivable                                                             | 5,858             | 4,783             |
| Other receivables                                                               | (2,729)           | (1,297)           |
| Inventories                                                                     | (12,845)          | (9,926)           |
| Prepaid expenses and other assets                                               | 4,052             | 1,758             |
| Accounts payable and accrued liabilities                                        | (501)             | (2,384)           |
| Income taxes payable                                                            | 2,761             | 3,546             |
| Postretirement health care benefits                                             | (233)             | 12                |
| Deferred compensation and other liabilities                                     | 584               | 282               |
| Net cash from operating activities                                              | 9,667             | 11,862            |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                    |                   |                   |
| Capital expenditures                                                            | (7,722)           | (4,845)           |
| Purchases of trading securities                                                 | (3,258)           | (2,584)           |
| Sales of trading securities                                                     | 239               | 435               |
| Purchase of available for sale securities                                       | (34,061)          | (27,227)          |
| Sale and maturity of available for sale securities                              | 11,670            | 1,759             |
| Net cash used in investing activities                                           | (33,132)          | (32,462)          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                    |                   |                   |
| Shares purchased and retired                                                    | (12,498)          | (9,985)           |
| Dividends paid in cash                                                          | (11,282)          | (11,128)          |
| Proceeds from bank loans                                                        | 641               | 324               |
| Repayment of bank loans                                                         | (661)             | (570)             |
| Net cash used in financing activities                                           | (23,800)          | (21,359)          |
| Effect of exchange rate changes on cash                                         | 829               | 1,376             |
| Decrease in cash and cash equivalents                                           | (46,436)          | (40,583)          |
| Cash, cash equivalents and restricted cash at beginning of year                 | 96,720            | 119,527           |
| Cash, cash equivalents and restricted cash at end of quarter                    | \$ 50,284         | \$ 78,944         |
| Supplemental cash flow information:                                             |                   |                   |

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|                                   |           |           |
|-----------------------------------|-----------|-----------|
| Income taxes paid/(received), net | \$ (206)  | \$ 784    |
| Interest paid                     | \$ 24     | \$ 14     |
| Stock dividend issued             | \$ 60,538 | \$ 69,739 |

(The accompanying notes are an integral part of these statements.)

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TOOTSIE ROLL INDUSTRIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2018

(in thousands except per share amounts) (Unaudited)

Note 1 — Significant Accounting Policies

General Information

Foregoing data has been prepared from the unaudited financial records of Tootsie Roll Industries, Inc. (the Company) and in the opinion of management all adjustments, which are of a normal recurring nature, necessary for a fair statement of the results for the interim period have been reflected. Certain amounts previously reported have been reclassified to conform to the current year presentation. These consolidated financial statements should be read in conjunction with the consolidated financial statements and the related notes included in the Company's Form 10-K for the year ended December 31, 2017 (the "2017 Form 10-K").

Results of operations for the period ended March 31, 2018 are not necessarily indicative of results to be expected for the year to end December 31, 2018 because of the seasonal nature of the Company's operations. Historically, the third quarter has been the Company's largest sales quarter due to pre-Halloween sales.

Revenue Recognition

The Company's revenues, primarily net product sales, principally result from the sale of goods, reflect the consideration to which the Company expects to be entitled generally based on customer purchase orders. The Company records revenue based on a five-step model in accordance with Accounting Standards Codification ("ASC") Topic 606 which became effective January, 1, 2018. Adjustments for estimated customer cash discounts upon payment, discounts for price adjustments, product returns, allowances, and certain advertising and promotional costs, including consumer coupons, are variable consideration and are recorded as a reduction of product sales revenue in the same period the related product sales are recorded. Such estimates are calculated using historical averages adjusted for any expected changes due to current business conditions and experience. A net product sale is recorded when the

Company delivers the product to the customer, or in certain instances, the customer picks up the goods at the Company's distribution center, and thereby obtains control of such product. Shipping and handling costs are included in selling, marketing and administrative expenses. Accounts receivable are unsecured. The Company does not have any significant licenses of intellectual property. See "Recently Adopted Accounting Pronouncements" for further discussion.

#### Recently Adopted Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, (ASC Topic 606) which supersedes nearly all existing revenue recognition guidance. Subsequent to the issuance of ASC Topic 606, the FASB clarified and amended the guidance through several Accounting Standard Updates; hereinafter the collection of revenue guidance is referred to as "ASC 606". The core principle of ASC 606 is that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Company adopted ASU 2014-09 and related amendments (ASC 606) as of January 1, 2018 using the modified retrospective method. As a result of adoption, the cumulative impact to retained earnings at January 1, 2018 was a net after-tax increase of \$3,319 (\$4,378 pre-tax). This adjustment principally changed the timing of recognition of certain trade promotions and related adjustments thereto which affect net product sales. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the impact of the adoption of the new standard to be immaterial to its net income on an ongoing basis. Revenue continues to be recognized at a point in time for product sales when products are delivered to or picked up by the customer as discussed above.

In February 2018, the FASB issued ASU 2018-02 which provides financial statement preparers with an option to reclassify stranded tax effects within Accumulated Other Comprehensive Income (AOCI) to retained earnings in each

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period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act (or portion thereof) is recorded. The guidance is effective for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted, including adoption in any interim period. The amendments should be applied either in the period adopted or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company early adopted ASU 2018-02 on January 1, 2018 with a \$593 cumulative-effect adjustment from AOCI to decrease retained earnings related to certain tax effects of unrealized gains and losses on available-for-sale securities and other post-retirement benefits. No other income tax effects related to the application of the Tax Cuts and Jobs Act were reclassified from AOCI to retained earnings.

In January 2016, the FASB issued ASU 2016-01, as amended by ASU 2018-03, issued in February 2018, which among other changes in accounting and disclosure requirements, replaces the cost method of accounting for non-marketable equity securities with a model for recognizing impairments and observable price changes, and also eliminates the available-for-sale classification for marketable equity securities. The Company adopted this guidance as of January 1, 2018. The Company does not have any non-marketable securities, and therefore, the adoption of this guidance did not have any impact on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, which clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows. The standard will be effective for fiscal years beginning after December 15, 2017, including interim periods within those years. The Company retrospectively adopted this guidance effective January 1, 2018. The Company's adoption of this guidance did not have a material impact on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18 which requires amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the total beginning and ending amounts for the periods shown on the statement of cash flows. The standard is effective for fiscal years beginning after December 15, 2017, including interim periods within those years using a retrospective transition method to each period presented. The Company retrospectively adopted this guidance as of January 1, 2018. The Company's adoption of this guidance did not have a material impact on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07 which requires companies with other postretirement employee benefit plans to present the service cost component of net periodic benefit cost in the same income statement line item as other compensation costs. The other components of net periodic benefit cost will be presented separately and not included in operating income. The standard will be effective for fiscal years beginning after December 15, 2017, including interim periods within those years. The Company retrospectively adopted this guidance effective January 1, 2018. The Company's adoption of this guidance did not have a material impact on its consolidated financial statements.

## Accounting Pronouncements

In February 2016, the FASB issued ASU 2016-02 which amends existing guidance to require lessees to recognize assets and liabilities on the balance sheet for the rights and obligations created by long-term leases and to disclose additional quantitative and qualitative information about leasing arrangements. This ASU also provides clarifications surrounding the presentation of the effects of leases in the income statement and statement of cash flows. This guidance will be effective for the Company on January 1, 2019. The Company is currently evaluating this new guidance to determine the impact it will have on its consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, guidance that amends hedge accounting. Under the new guidance, more hedging strategies will be eligible for hedge accounting and the application of hedge accounting is simplified. The new guidance amends presentation and disclosure requirements, and how effectiveness is assessed. The guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those years. Early adoption is permitted. The Company is currently evaluating the impact that the new guidance will have on its consolidated financial statements.

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Note 2 — Average Shares Outstanding

The average number of shares outstanding for three months 2018 reflects stock purchases of 361 shares for \$12,498 and a 3% stock dividend of 1,869 shares distributed on April 6, 2018. The average number of shares outstanding for three months 2017 reflects stock purchases of 260 shares for \$9,985 and a 3% stock dividend of 1,847 shares distributed on April 17, 2017.

Note 3 — Income Taxes

The Company is subject to taxation in the U.S. and various state and foreign jurisdictions. The Company remains subject to examination by U.S. federal and state and foreign tax authorities for the years 2014 through 2016. With few exceptions, the Company is no longer subject to examination by tax authorities for the year 2013 and prior. The consolidated effective tax rates were 21.8% and 29.3% in first quarter 2018 and 2017, respectively. The lower effective tax rate for first quarter 2018 compared to first quarter 2017 principally reflects the lower federal tax rate of 21% effective for 2018.

The Company believes it has obtained and analyzed all reasonably available information necessary to record the effects of the change in tax law and considers its accounting for the effects of the 2017 Tax Reform Act to be provisional as of March 31, 2018. The ultimate impact may differ from these provisional amounts, possibly materially, due to, among other things, additional regulatory guidance that may be issued by the Internal Revenue Service, and actions the Company may take as a result of the Tax Reform Act.

Note 4 — Fair Value Measurements

Current accounting guidance defines fair value as the price that would be received on the sale of an asset, or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Guidance requires disclosure of the extent to which fair value is used to measure financial assets and liabilities, the inputs utilized in calculating valuation measurements, and the effect of the measurement of significant unobservable inputs on earnings, or changes in net assets, as of the measurement date. Guidance establishes a three-level valuation hierarchy based upon the transparency of inputs utilized in the measurement and valuation of financial assets or liabilities as of the measurement date. Level 1 inputs include quoted prices for identical instruments and are the most observable. Level 2 inputs include quoted prices for similar assets and observable inputs such as interest rates, foreign currency exchange rates, commodity rates and yield curves. Level 3 inputs are not observable in the market and include management's own judgments about the assumptions market participants would use in pricing the asset or liability. The use of observable and unobservable inputs is reflected in the hierarchy assessment disclosed in the table below.

As of March 31, 2018, December 31, 2017 and March 31, 2017, the Company held certain financial assets that are required to be measured at fair value on a recurring basis. These included derivative hedging instruments related to the purchase of certain raw materials and foreign currencies, investments in trading securities and available for sale securities. The Company's available for sale securities principally consist of corporate and municipal bonds that are publicly traded and variable rate demand notes with interest rates that generally reset weekly and the security can be "put" back and sold weekly. Trading securities principally consist of equity mutual funds that are publicly traded.

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The following table presents information about the Company's financial assets and liabilities measured at fair value as of March 31, 2018, December 31, 2017 and March 31, 2017 and indicate the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value:

|                                     | Estimated Fair Value March 31, 2018 |                   |            |         |
|-------------------------------------|-------------------------------------|-------------------|------------|---------|
|                                     | Total                               | Input Levels Used |            |         |
|                                     | Fair Value                          | Level 1           | Level 2    | Level 3 |
| Cash and cash equivalents           | \$ 49,867                           | \$ 49,867         | \$ -       | \$ -    |
| Available for sale securities       | 192,712                             | -                 | 192,712    | -       |
| Foreign currency forward contracts  | 21                                  | -                 | 21         | -       |
| Commodity futures contracts         | (1,095)                             | (1,095)           | -          | -       |
| Trading securities                  | 63,520                              | 63,520            | -          | -       |
| Total assets measured at fair value | \$ 305,025                          | \$ 112,292        | \$ 192,733 | \$ -    |

  

|                                     | Estimated Fair Value December 31, 2017 |                   |            |         |
|-------------------------------------|----------------------------------------|-------------------|------------|---------|
|                                     | Total                                  | Input Levels Used |            |         |
|                                     | Fair Value                             | Level 1           | Level 2    | Level 3 |
| Cash and cash equivalents           | \$ 96,314                              | \$ 96,314         | \$ -       | \$ -    |
| Available for sale securities       | 171,596                                | 1,200             | 170,396    | -       |
| Foreign currency forward contracts  | 79                                     | -                 | 79         | -       |
| Commodity futures contracts, net    | 32                                     | 32                | -          | -       |
| Trading securities                  | 60,520                                 | 60,520            | -          | -       |
| Total assets measured at fair value | \$ 328,541                             | \$ 158,066        | \$ 170,475 | \$ -    |

  

|                                     | Estimated Fair Value March 31, 2017 |                   |            |         |
|-------------------------------------|-------------------------------------|-------------------|------------|---------|
|                                     | Total                               | Input Levels Used |            |         |
|                                     | Fair Value                          | Level 1           | Level 2    | Level 3 |
| Cash and cash equivalents           | \$ 78,555                           | \$ 78,555         | \$ -       | \$ -    |
| Available for sale securities       | 189,289                             | 2,412             | 186,877    | -       |
| Foreign currency forward contracts  | (71)                                | -                 | (71)       | -       |
| Commodity futures contracts         | 26                                  | 26                | -          | -       |
| Trading securities                  | 73,025                              | 73,025            | -          | -       |
| Total assets measured at fair value | \$ 340,824                          | \$ 154,018        | \$ 186,806 | \$ -    |

The fair value of the Company's industrial revenue development bonds at March 31, 2018, December 31, 2017 and March 31, 2017 were valued using Level 2 inputs which approximates the carrying value of \$7,500 for the respective periods. Interest rates on these bonds are reset weekly based on current market conditions.

## Note 5 — Derivative Instruments and Hedging Activities

The Company uses derivative instruments, including foreign currency forward contracts, commodity futures contracts and commodity option contracts, to manage its exposures to foreign exchange and commodity prices. Commodity futures contracts and most commodity option contracts are intended and effective as hedges of market price risks associated with the anticipated purchase of certain raw materials (primarily sugar). Foreign currency forward contracts are intended and effective as hedges of the Company's exposure to the variability of cash flows, primarily related to the foreign exchange rate changes of products manufactured in Canada and sold in the United States. The Company does not engage in trading or other speculative use of derivative instruments.

The Company recognizes all derivative instruments as either assets or liabilities at fair value in the Condensed Consolidated Statement of Financial Position. Derivative assets are recorded in other receivables and derivative liabilities are recorded in accrued liabilities. The Company uses hedge accounting for its foreign currency and commodity derivative instruments as discussed above. Derivatives that qualify for hedge accounting are designated as cash flow hedges by formally documenting the hedge relationships, including identification of the hedging

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instruments, the hedged items and other critical terms, as well as the Company's risk management objectives and strategies for undertaking the hedge transaction.

Changes in the fair value of the Company's cash flow hedges are recorded in accumulated other comprehensive loss, net of tax, and are reclassified to earnings in the periods in which earnings are affected by the hedged item.

Substantially all amounts reported in accumulated other comprehensive loss for commodity derivatives are expected to be reclassified to cost of goods sold. Approximately \$836 of this accumulated comprehensive loss is expected to be reclassified to earnings in 2018 and a \$259 accumulated comprehensive loss is expected to be reclassified as a charge to earnings in 2019. Substantially all amounts reported in accumulated other comprehensive loss for foreign currency derivatives are expected to be reclassified to other income, net in 2018.

The following table summarizes the Company's outstanding derivative contracts and their effects on its Condensed Consolidated Statements of Financial Position at March 31, 2018, December 31, 2017 and March 31, 2017:

|                                                | March 31, 2018      |        |             |
|------------------------------------------------|---------------------|--------|-------------|
|                                                | Notional<br>Amounts | Assets | Liabilities |
| Derivatives designated as hedging instruments: |                     |        |             |
| Foreign currency forward contracts             | \$ 368              | \$ 21  | \$ -        |
| Commodity futures contracts                    | 11,537              | 5      | (1,100)     |
| Total derivatives                              |                     | \$ 26  | \$ (1,100)  |
|                                                |                     |        |             |
|                                                | December 31, 2017   |        |             |
|                                                | Notional<br>Amounts | Assets | Liabilities |
| Derivatives designated as hedging instruments: |                     |        |             |
| Foreign currency forward contracts             | \$ 919              | \$ 79  | \$ -        |
| Commodity futures contracts                    | 13,840              | 284    | (252)       |
| Total derivatives                              |                     | \$ 363 | \$ (252)    |
|                                                |                     |        |             |
|                                                | March 31, 2017      |        |             |
|                                                | Notional<br>Amounts | Assets | Liabilities |
| Derivatives designated as hedging instruments: |                     |        |             |
| Foreign currency forward contracts             | \$ 1,768            | \$ -   | \$ (71)     |
| Commodity futures contracts                    | 9,880               | 673    | (647)       |
| Total derivatives                              |                     | \$ 673 | \$ (718)    |



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The effects of derivative instruments on the Company's Condensed Consolidated Statements of Earnings and Retained Earnings and the Condensed Consolidated Statements of Comprehensive Earnings for periods ended March 31, 2018 and March 31, 2017 are as follows:

| For Quarter Ended March 31, 2018   |                                        |                                                                      |                                                                                              |
|------------------------------------|----------------------------------------|----------------------------------------------------------------------|----------------------------------------------------------------------------------------------|
|                                    | Gain<br>(Loss)<br>Recognized<br>in OCI | Gain (Loss)<br>Reclassified from<br>Accumulated OCI<br>into Earnings | Gain (Loss)<br>on Amount Excluded<br>from Effectiveness<br>Testing Recognized<br>in Earnings |
| Foreign currency forward contracts | \$ (11)                                | \$ 47                                                                | \$ -                                                                                         |
| Commodity futures contracts        | (1,461)                                | (334)                                                                | -                                                                                            |
| Total                              | \$ (1,472)                             | \$ (287)                                                             | \$ -                                                                                         |
| For Quarter Ended March 31, 2017   |                                        |                                                                      |                                                                                              |
|                                    | Gain<br>(Loss)<br>Recognized<br>in OCI | Gain (Loss)<br>Reclassified from<br>Accumulated OCI<br>into Earnings | Gain (Loss)<br>on Amount Excluded<br>from Effectiveness<br>Testing Recognized<br>in Earnings |
| Foreign currency forward contracts | \$ 23                                  | \$ (25)                                                              | \$ -                                                                                         |
| Commodity futures contracts        | (573)                                  | 1,147                                                                | -                                                                                            |
| Total                              | \$ (550)                               | \$ 1,122                                                             | \$ -                                                                                         |

## Note 6 — Pension Plans

During 2018 and 2017, the Company received updated notices that the Bakery and Confectionery Union and Industry International Pension Plan (Plan), a multi-employer defined benefit pension plan for certain Company union employees, is in "critical and declining status", as defined by the Pension Protection Act (PPA) and the Pension Benefit Guaranty Corporation (PBGC), and that the Plan is projected to become insolvent in 2030. The Company has been advised that its withdrawal liability would have been \$82,200 if it had withdrawn from the Plan during 2017. Should the Company actually withdraw from the Plan at a future date, a withdrawal liability, which could be higher than the above discussed amount, could be payable to the Plan.

The Company is currently unable to determine the ultimate outcome of the above discussed matter and therefore, is unable to determine the effects on its consolidated financial statements, but the ultimate outcome or the effects of any modifications to the current rehabilitation plan and possible new “hybrid plan” option discussed in Management’s Discussion and Analysis of Financial Condition and Results of Operations (Item 2) could be material to its consolidated results of operations or cash flows in one or more future periods. See also the Company’s Consolidated Financial Statements and related notes and Management’s Discussion and Analysis of Financial Condition and Results of Operations incorporated into the Company’s 2017 Form 10-K.

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## Note 7 — Accumulated Other Comprehensive Earnings (Loss)

Accumulated Other Comprehensive Earnings (Loss) consists of the following components:

|                                                                    | Foreign<br>Currency<br>Translation | Investments | Foreign<br>Currency<br>Derivatives | Commodity<br>Derivatives | Postretirement<br>and Pension<br>Benefits | Accumulated<br>Other<br>Comprehensive<br>Earnings (Loss) |
|--------------------------------------------------------------------|------------------------------------|-------------|------------------------------------|--------------------------|-------------------------------------------|----------------------------------------------------------|
| Balance at<br>December 31, 2017                                    | \$ (24,262)                        | \$ (889)    | \$ 51                              | \$ 20                    | \$ 3,289                                  | \$ (21,791)                                              |
| Other comprehensive<br>earnings (loss) before<br>reclassifications | 1,612                              | (948)       | (8)                                | (1,107)                  | -                                         | (451)                                                    |
| Reclassifications from<br>accumulated other<br>comprehensive loss  | -                                  | -           | (36)                               | 253                      | (251)                                     | (34)                                                     |
| Other comprehensive<br>earnings (loss) net of<br>tax               | 1,612                              | (948)       | (44)                               | (854)                    | (251)                                     | (485)                                                    |
| Adoption of ASU<br>2018-02 (See Note 1)                            | -                                  | (168)       | 9                                  | 4                        | 748                                       | 593                                                      |
| Balance at March 31,<br>2018                                       | \$ (22,650)                        | \$ (2,005)  | \$ 16                              | \$ (830)                 | \$ 3,786                                  | \$ (21,683)                                              |
|                                                                    | Foreign<br>Currency<br>Translation | Investments | Foreign<br>Currency<br>Derivatives | Commodity<br>Derivatives | Postretirement<br>and Pension<br>Benefits | Accumulated<br>Other<br>Comprehensive<br>Earnings (Loss) |
| Balance at<br>December 31, 2016                                    | \$ (25,460)                        | \$ (697)    | \$ (76)                            | \$ 1,114                 | \$ 4,873                                  | \$ (20,246)                                              |
| Other comprehensive<br>earnings (loss) before<br>reclassifications | 2,100                              | 148         | 15                                 | (366)                    | 4                                         | 1,901                                                    |
| Reclassifications from<br>accumulated other<br>comprehensive loss  | -                                  | -           | 16                                 | (732)                    | (233)                                     | (949)                                                    |
| Other comprehensive<br>earnings (loss) net of<br>tax               | 2,100                              | 148         | 31                                 | (1,098)                  | (229)                                     | 952                                                      |
| Balance at March 31,<br>2017                                       | \$ (23,360)                        | \$ (549)    | \$ (45)                            | \$ 16                    | \$ 4,644                                  | \$ (19,294)                                              |

The amounts reclassified from accumulated other comprehensive income (loss) consisted of the following:

| Details about Accumulated Other<br>Comprehensive Income Components | Quarter Ended     |                   | Location of (Gain) Loss                     |
|--------------------------------------------------------------------|-------------------|-------------------|---------------------------------------------|
|                                                                    | March<br>31, 2018 | March 31,<br>2017 |                                             |
| Foreign currency derivatives                                       | \$ (47)           | \$ 25             | Recognized in Earnings<br>Other income, net |
| Commodity derivatives                                              | 334               | (1,147)           | Product cost of goods sold                  |
| Postretirement and pension benefits                                | (331)             | (365)             | Other income, net                           |
| Total before tax                                                   | (44)              | (1,487)           |                                             |
| Tax (expense) benefit                                              | 10                | 538               |                                             |
| Net of tax                                                         | \$ (34)           | \$ (949)          |                                             |

#### Note 8 — Restricted Cash

Restricted cash comprises certain cash deposits of the Company's majority-owned Spanish companies with international banks that are pledged as collateral for letters of credit and bank borrowings.

#### Note 9 — Bank Loans

Bank loans comprise borrowings by the Company's majority-owned Spanish companies which are held by international banks.

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

This financial review discusses the Company's financial condition, results of operations, liquidity and capital resources and other matters. Dollars are presented in thousands, except per share amounts. This review should be read in conjunction with the accompanying Condensed Consolidated Financial Statements and related notes included in this Form 10-Q and with the Company's Consolidated Financial Statements and related notes and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Form 10-K for the year ended December 31, 2017 (the "2017 Form 10-K").

Net product sales were \$100,859 in first quarter 2018 compared to \$103,425 in first quarter 2017, a decrease of \$2,566 or 2.5%. Lower price realization and declines in sales from exports and foreign subsidiaries contributed to the decline in net product sales in first quarter 2018 compared to first quarter 2017. Lower price realization in first quarter 2018 principally reflects increases in trade promotions and consumer coupon programs. More favorable foreign exchange, which reflects a weaker U.S. dollar, had some favorable impact on first quarter 2018 net product sales when compared to first quarter 2017.

Product cost of goods sold were \$65,834 in first quarter 2018 compared to \$65,538 in first quarter 2017. Product cost of goods sold includes \$14 and \$787 of certain deferred compensation expenses in first quarter 2018 and 2017, respectively. These deferred compensation expenses principally result from the changes in the market value of investments and investment income from trading securities relating to compensation deferred in previous years and are not reflective of current operating results. Adjusting for the aforementioned, product cost of goods sold increased from \$64,751 in first quarter 2017 to \$65,820 in first quarter 2018, an increase of \$1,069 or 1.7%. As a percentage of net product sales, adjusted product cost of goods sold was 65.3% and 62.6% in first quarter 2018 and 2017, respectively, an unfavorable increase of 2.7 percentage points. Adjusted cost of goods sold in first quarter includes higher manufacturing plant overhead costs, principally increases in plant repairs and maintenance and plant utilities, and increases in employee healthcare and other benefit costs resulting from unfavorable experience and higher resulting claims costs under the Company's self-insured programs. Overall ingredient costs were more favorable in first quarter 2018 compared to first quarter 2017, although some ingredient costs were higher.

Margins were also adversely affected by additional costs and expenses relating to changes in, and start-up of new manufacturing packaging lines which are scheduled to be phased into service during the second and third quarters of 2018. The Company is continuing its investments in its plant manufacturing operations to meet new consumer and customer demands, achieve quality improvements, and increase operational efficiencies. Plant efficiencies driven by capital investments and ongoing cost containment programs mitigated some of the higher costs and expenses

discussed above.

Selling, marketing and administrative expenses were \$25,857 in first quarter 2018 compared to \$26,725 in first quarter 2017. Selling, marketing and administrative expenses includes \$397 and \$2,095 of certain deferred compensation expenses in first quarter 2018 and 2017. As discussed above, these expenses principally result from changes in the market value of investments and investment income from trading securities relating to compensation deferred in previous years, and are not reflective of current operating results. Adjusting for the aforementioned, selling, marketing and administrative expenses increased from \$24,630 in first quarter 2017 to \$25,460 in first quarter 2018, an increase of \$830 or 3.4%. As a percentage of net product sales, adjusted selling, marketing and administrative expenses increased from 23.8% in first quarter 2017 to 25.2% in 2018, an unfavorable increase of 1.4 percentage points as a percent of net sales.

Selling, marketing and administrative expenses include \$10,220 and \$9,695 for customer freight, delivery and warehousing expenses in first quarter 2018 and 2017, respectively. These expenses were 10.1% and 9.4% of net product sales in first quarter 2018 and 2017, respectively, and contributed to the increase in 2018 adjusted selling, marketing and administrative expenses. Increased freight and delivery expenses reflects higher freight rates principally due to increases in fuel costs and the continuing imbalance between supply and demand for over-the-road truck

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delivery. Much of this imbalance is being driven by a nationwide driver shortage as well as new federal regulations which require increased monitoring of a driver's allowed driving time using electronic monitoring technology.

Earnings from operations were \$9,842 in first quarter 2018 compared to \$11,926 in first quarter 2017. Earnings from operations include \$411 and \$2,882 of certain deferred compensation expenses in first quarter 2018 and 2017, respectively, which are discussed above. Adjusting for these deferred compensation costs and expenses, operating earnings were \$10,253 and \$14,808 in first quarter 2018 and 2017, respectively, a decrease of \$4,555 or 30.8%. As a percentage of net product sales, these adjusted operating earnings were 10.2% and 14.3% in first quarter 2018 and 2017, respectively, an unfavorable decrease of 4.1% as a percentage of net product sales. This decline in operating earnings principally reflects the adverse effects of lower sales, higher plant manufacturing overhead and employee benefit costs, and increases in customer freight and delivery expenses as discussed above. Less favorable results from the Company's foreign subsidiaries and the effects of lower export sales also adversely affected first quarter 2018 operating income compared to first quarter 2017. Management believes the presentation in this and the preceding paragraphs relating to amounts adjusted for deferred compensation expense are more reflective of the underlying operations of the Company.

Other income, net was \$521 in first quarter 2018 compared to \$2,228 in first quarter 2017, an unfavorable decrease of \$1,707. Other income, net for first quarter 2018 and 2017 includes net gains and investment income of \$411 and \$2,882, respectively, on trading securities which provide an economic hedge of the Company's deferred compensation liabilities. These changes in trading securities were substantially offset by a like amount of deferred compensation expense included in product cost of goods sold and selling, marketing, and administrative expenses in the respective periods as discussed above. Other income, net includes gains (losses) on foreign exchange of \$(904) and \$(1,545) in first quarter 2018 and 2017, respectively.

The consolidated effective tax rates were 21.8% and 29.3% in first quarter 2018 and 2017, respectively. The lower effective tax rate for first quarter 2018 compared to first quarter 2017 principally reflects the lower U.S. federal income tax rate resulting from U.S. tax legislation enacted in December 2017.

Net earnings attributable to Tootsie Roll Industries, Inc. were \$8,125 (after \$24 net loss attributed to non-controlling interests) in first quarter 2018 compared to \$10,051 (after \$40 net loss attributed to non-controlling interests) in first quarter 2017, and earnings per share were \$0.13 and \$0.15 in first quarter 2018 and 2017, respectively, a decrease of \$0.02 per share, or 13%. Earnings per share attributable to Tootsie Roll Industries, Inc. for first quarter 2018 did benefit from the reduction in average shares outstanding resulting from purchases in the open market by the Company of its common stock. Average shares outstanding decreased from 65,474 in first quarter 2017 to 64,434 in first quarter 2018.

Goodwill and intangibles are assessed annually as of December 31 or whenever events or circumstances indicate that the carrying values may not be recoverable from future cash flows. The Company has not identified any triggering events, as defined, or other adverse information that would indicate a material impairment of its goodwill or

intangibles in first quarter 2018. There were also no impairments in the comparative first quarter 2017 period or in calendar 2017.

As more fully discussed in Note 1, the Company adopted the new accounting revenue recognition guidance (ASC 606) effective January 1, 2018. As a result of adoption, the cumulative impact to retained earnings at January 1, 2018 was a net after-tax increase of \$3,319 (\$4,378 pre-tax). This adjustment to retained earnings principally changed the timing of recognition of certain trade promotions and related adjustments thereto which affect net product sales. The comparative first quarter 2017 information has not been restated and continues to be reported under the accounting standards in effect for such period. The Company expects the impact of the adoption of the new standard to be immaterial to its net income in calendar 2018 and future years. Revenue for net product sales continues to be recognized at a point in time when products are delivered to or picked up by the customer, as designated by customers' purchase orders, as discussed in Note 1.

Beginning in 2012, the Company received periodic notices from the Bakery and Confectionery Union and Industry International Pension Plan (Plan), a multi-employer defined benefit pension plan for certain Company union employees, that the Plan's actuary certified the Plan to be in "critical status", the "Red Zone", as defined by the Pension Protection Act (PPA) and the Pension Benefit Guaranty Corporation (PBGC), and that a plan of rehabilitation was adopted by the trustees of the Plan in 2012 (and was further amended in 2016). During 2015, the Company received

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notices that the Plan's status was changed to "critical and declining status", as defined by the PPA and PBGC, for the plan year beginning January 1, 2015, and that the Plan was projected to have an accumulated funding deficiency for the 2017 through 2024 plan years. A designation of "critical and declining status" implies that the Plan is expected to become insolvent in the next 20 years. In April 2018, the Company received new updated notices that the Plan remains in "critical and declining status" and is projected to become insolvent in 2030. These notices also advise that the Plan trustees have updated the Rehabilitation Plan and are considering the reduction or elimination of certain retirement benefits with the goal of avoiding insolvency, and may ultimately seek assistance from the PBGC.

Based on updated annual notices, the Plan's funded percentages (plan investment assets as a percentage of plan liabilities), as defined, were 54.7%, 57.0% and 62.8% as of January 1, 2017 (most recent valuation date available), 2016, and 2015, respectively (these valuation dates are as of the beginning of each Plan year). These funded percentages are based on actuarial values, as defined, and do not reflect the actual market value of Plan investments as of these dates. If the market value of investments had been used as of January 1, 2017, the funded percentage would be 52.5% (not 54.7%). As of the January 1, 2017 valuation date (most recent valuation available), 19% of Plan participants were current active employees, 52% were retired or separated from service and receiving benefits, and 29% were retired or separated from service and entitled to future benefits. The number of current active employee Plan participants as of January 1, 2017 fell 8% from the previous year and 9% over the past two years. When compared to the Plan valuation date of January 1, 2011 (six years earlier), current active employees participants have declined 36%, whereas participants who were retired or separated from service and receiving benefits increased 6% and participants who were retired or separated from service and entitled to future benefits increased 8%. The bankruptcy of a major participating employer in the Plan contributed to the above discussed Plan results. The Internal Revenue Service recently issued updated mortality tables (increasing life expectancy) effective January 1, 2018 which will likely increase the Plan's liabilities and further decrease the above discussed funding percentages.

The Company has been advised that its withdrawal liability would have been \$82,200, \$72,700, and \$61,000 if it had withdrawn from the Plan during 2017, 2016 and 2015, respectively. The increase from 2016 to 2017 principally reflects a decrease in the PBGC interest rates, a decrease in the Plan's assets and an increase in the Plan's unfunded vested benefits during 2016 with the Company comprising an increasing proportion of the Plan's employer contribution base. Based on the above, including the Plan's projected insolvency in the year 2030, management believes that the Company's withdrawal liability will likely increase further in future years. Based on the Company's actuarial study and certain provisions in ERISA and the law relating to withdrawal liability payments, management believes that the Company's liability would likely be limited to twenty annual payments of \$3,059 which have a present value in the range of \$35,900 to \$46,900 depending on the interest rate used to discount these payments. The aforementioned is based on a range of valuation interest rates which management understands is provided under the statute. Should the Company actually withdraw from the Plan at a future date, a withdrawal liability, which could be higher than the above discussed amounts, could be payable to the Plan.

The Company and the union are currently in labor contract negotiations and are continuing to operate under extensions of the recently expired contract which requires the Company's continued participation in this Plan. The amended rehabilitation plan, which continues, requires that employer contributions include 5% compounded annual surcharge increases each year for an unspecified period of time beginning in 2012 as well as certain plan benefit reductions. The Company's pension expense for this Plan for calendar 2017 and 2016 was \$2,617 and \$2,541, respectively. The aforementioned expense includes surcharges of \$656 and \$542 in 2017 and 2016, respectively, as

required under the plan of rehabilitation as amended. The Company's pension expense for this Plan for first quarter 2018 and 2017 was \$553 and \$495 respectively, which includes surcharges of \$158 and \$124 respectively.

The Company is currently unable to determine the ultimate outcome of the above discussed matter and, therefore, is unable to determine the effects on its consolidated financial statements, but the ultimate outcome or the effects of any modifications to the current rehabilitation plan could be material to its consolidated results of operations or cash flows in one or more future periods. See also the Company's Consolidated Financial Statements and related notes and Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's 2017 Form 10-K.

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LIQUIDITY AND CAPITAL RESOURCES

Net cash flows provided by operating activities were \$9,667 and \$11,862 in first quarter 2018 and 2017, respectively, a decrease of \$2,195. The decrease in first quarter 2018 cash flows from operating activities principally reflects lower net earnings as discussed above, and the comparative effects of changes in inventories and other receivables offset by increases in accounts payable and accrued liabilities. The changes in inventories and accounts payable and accrued liabilities principally reflect the timing of purchases of packaging and ingredient inventory, production, sales and vendor payments, and the change in other receivables is primarily due to increased broker margin deposit requirements on commodity sugar hedges.

Net cash used in investing activities was \$33,132 in first quarter 2018 compared to \$32,462 in first quarter 2017. Cash flows from investing activities reflect \$34,061 and \$27,227 of purchases of available for sale securities during first quarter 2018 and 2017, respectively, and \$11,670 and \$1,759 of sales and maturities of available for sale securities during first quarter 2018 and 2017, respectively. First quarters 2018 and 2017 investing activities include capital expenditures of \$7,722 and \$4,845, respectively. All capital expenditures in 2018 are expected to be funded from the Company's cash flow from operations and internal sources. In addition, Company management has committed approximately \$13,000 to new manufacturing packaging lines at several manufacturing plants, and \$15,000 to a manufacturing plant rehabilitation upgrade and expansion of one of its manufacturing facilities in the U.S.A. Management expects to make substantially all of the cash outlays for the aforementioned packaging lines in 2018, and expects the projected cash outlays for the plant rehabilitation project to be approximately \$500 in 2018, \$7,000 in 2019 and \$7,500 in 2020.

The Company's consolidated financial statements include bank borrowings of \$425 and \$330 at March 31, 2018 and 2017, respectively, all of which relates to its two majority-owned and controlled Spanish companies. The Company had no other outstanding bank borrowings at March 31, 2018.

Financing activities include Company common stock purchases and retirements of \$12,498 and \$9,985 in three months 2018 and 2017, respectively. Cash dividends of \$11,282 and \$11,128 were paid in three months 2018 and 2017, respectively.

The Company's current ratio (current assets divided by current liabilities) was 4.6 to 1 at March 31, 2018 compared to 4.2 to 1 at December 31, 2017 and 4.5 to 1 at March 31, 2017. Net working capital was \$193,918 at March 31, 2018 compared to \$207,132 and \$202,749 at December 31, 2017 and March 31, 2017, respectively, the aforementioned net working capital amounts are principally reflected in aggregate cash and cash equivalents and short-term investments of \$110,188 at March 31, 2018 compared to \$137,920 and \$145,557 at December 31, 2017 and March 31, 2017, respectively. In addition, long term investments, principally debt securities comprising corporate and municipal bonds were \$195,911 at March 31, 2018, as compared to \$190,510 and \$195,312 at December 31, 2017 and March 31, 2017, respectively. Aggregate cash and cash equivalents and short and long-term investments were \$306,099, \$328,430, and \$340,869, at March 31, 2018, December 31, 2017 and March 31, 2017, respectively. The aforementioned includes

\$63,520, \$60,520, and \$73,025 at March 31, 2018, December 31, 2017 and March 31, 2017, respectively, relating to trading securities which are used as an economic hedge for the Company's deferred compensation liabilities. Investments in corporate and municipal bonds, variable rate demand notes, and other debt securities that matured during first quarter 2018 and 2017 were generally used to purchase the Company's common stock or were replaced with debt securities of similar maturities.

The Company periodically contributes to a VEBA trust, managed and controlled by the Company, to fund the estimated future costs of certain employee health, welfare and other benefits. The Company is currently using these VEBA funds to pay the actual cost of such benefits through most of 2022. The VEBA trust held \$18,654, \$19,713 and \$1,855 of aggregate cash and cash equivalents at March 31, 2018, December 31, 2017 and March 31, 2017, respectively. The Company contributed \$20,024 to this VEBA trust in fourth quarter 2017. This asset value is included in prepaid expenses and long-term other assets in the Company's Consolidated Statement of Financial Position. These assets are categorized as Level 2 within the fair value hierarchy.

#### ACCOUNTING PRONOUNCEMENTS

See Note 1 of the Company's condensed consolidated financial statements.

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RISK FACTORS

There were no material changes to the risk factors disclosed in the Company's 2017 Form 10-K.

FORWARD-LOOKING STATEMENTS

This discussion and certain other sections contain forward-looking statements that are based largely on the Company's current expectations and are made pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995. Forward-looking statements can be identified by the use of words such as "anticipated," "believe," "expect," "intend," "estimate," "project," "plan" and other words of similar meaning in connection with a discussion of future operating or financial performance and are subject to certain factors, risks, trends and uncertainties that could cause actual results and achievements to differ materially from those expressed in the forward-looking statements. Such factors, risks, trends and uncertainties, which in some instances are beyond the Company's control, include the overall competitive environment in the Company's industry, changes in assumptions and judgments discussed above under the heading "Significant Accounting Policies and Estimates," and factors identified and referred to above under the heading "Risk Factors" in this report and under the heading "Risk Factors" in the Company's 2017 Form 10-K.

The risk factors identified and referred to above are believed to be significant factors, but not necessarily all of the significant factors that could cause actual results to differ from those expressed in any forward-looking statement. Readers are cautioned not to place undue reliance on such forward-looking statements, which are made only as of the date of this report. The Company undertakes no obligation to update such forward-looking statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company is exposed to various market risks, including fluctuations in and sufficient availability of sugar, corn syrup, edible oils, including palm oils, cocoa, dextrose, milk and whey, and gum-base input ingredients and packaging, and fuel costs principally relating to freight and delivery fuel surcharges. The Company is exposed to exchange rate fluctuations in the Canadian dollar which is the currency used for a portion of the raw material and packaging material costs and all labor, benefits and local plant operating costs at its Canadian plants. The Company is exposed to exchange rate fluctuations in Mexico, Canada, and Spain where its subsidiaries sell products in their local currencies. The Company invests in securities with maturities dates of up to approximately three years which are generally held to maturity, and variable rate demand notes where interest rates are generally reset weekly, all of which limits the Company's exposure to interest rate fluctuations. There have been no material changes in the Company's market risks that would significantly affect the disclosures made in the Form 10-K for the year ended December 31, 2017.

#### ITEM 4. CONTROLS AND PROCEDURES

Under the supervision and with the participation of management, the Chief Executive Officer and Chief Financial Officer of the Company have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of March 31, 2018 and, based on their evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these controls and procedures are effective. Disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures are also designed to ensure that information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting that occurred during the Company's fiscal quarter ended March 31, 2018 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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## PART II — OTHER INFORMATION

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table summarizes the Company's purchases of its common stock during the quarter ended March 31, 2018:

| Period          | (a) Total<br>Number of<br>Shares<br>Purchased | (b) Average<br>Price Paid per<br>Share | Shares<br>Purchased as Part of<br>Publicly Announced Plans<br>Or Programs | Approximate Dollar<br>Value of Shares that<br>May Yet Be Purchased<br>Under the Plans<br>or Programs |
|-----------------|-----------------------------------------------|----------------------------------------|---------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------|
| Jan 1 to Jan 31 | 172,915                                       | \$ 35.85                               | Not Applicable                                                            | Not Applicable                                                                                       |
| Feb 1 to Feb 28 | 94,335                                        | 34.69                                  | Not Applicable                                                            | Not Applicable                                                                                       |
| Mar 1 to Mar 31 | 93,888                                        | 32.07                                  | Not Applicable                                                            | Not Applicable                                                                                       |
| Total           | 361,138                                       | \$ 34.57                               | Not Applicable                                                            | Not Applicable                                                                                       |

While the Company does not have a formal or publicly announced stock purchase program, the Company's board of directors periodically authorizes a dollar amount for share purchases. The treasurer executes share purchase transactions according to these guidelines.

## ITEM 6. EXHIBITS

Exhibits 31.1 — Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibits 31.2 — Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 32 — Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 101.INS - XBRL Instance Document.

Exhibit 101.SCH - XBRL Taxonomy Extension Schema Document.

Exhibit 101.CAL - XBRL Taxonomy Extension Calculation Linkbase Document.

Exhibit 101.LAB - XBRL Taxonomy Extension Label Linkbase Document.

Exhibit 101.PRE - XBRL Taxonomy Extension Presentation Linkbase Document.

Exhibit 101.DEF - XBRL Taxonomy Extension Definition Linkbase Document.

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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.

TOOTSIE ROLL  
INDUSTRIES, INC.

Date: May 10, 2018    BY: /S/ELLEN R. GORDON  
Ellen R. Gordon  
Chairman and Chief  
Executive Officer

Date: May 10, 2018    BY: /S/G. HOWARD EMBER, JR.  
G. Howard Ember, Jr.  
Vice President Finance and  
Chief Financial Officer