

**SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-K**

**FOR ANNUAL AND TRANSITION REPORTS  
PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2007

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-4776

**STURM, RUGER & COMPANY, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**06-0633559**

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

**Lacey Place, Southport, Connecticut**

(Address of Principal Executive Offices)

**06890**

(Zip Code)

**(203) 259-7843**

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of Each Class                | Name of Each Exchange on Which Registered |
|------------------------------------|---|
| <b>Common Stock, \$1 par value</b> | <b>New York Stock Exchange</b>            |

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [  ].

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. Large accelerated filer [  ] Accelerated filer [  ] Non-accelerated filer [  ].

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of June 30, 2007:

*Common Stock, \$1 par value - \$351,994,000*

The number of shares outstanding of the registrant's common stock as of February 15, 2008:

*Common Stock, \$1 par value - 20,788,000 shares*

**DOCUMENTS INCORPORATED BY REFERENCE.**

Portions of the registrant's Proxy Statement relating to its 2008 Annual Stockholders' meeting, to be filed subsequently are incorporated by reference into Part III of this Report.

Portions of the registrant's Proxy Statement relating to the 2008 Annual Meeting of Stockholders to be held April 23, 2008 are incorporated by reference into Part III (Items 10 through 14) of this Report.

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In this Annual Report on Form 10-K, Sturm, Ruger & Company, Inc. (the “Company”) makes forward-looking statements and projections concerning future expectations. Such statements are based on current expectations and are subject to certain qualifying risks and uncertainties, such as market demand, sales levels of firearms, anticipated castings sales and earnings, the need for external financing for operations or capital expenditures, the results of pending litigation against the Company including lawsuits filed by mayors, attorneys general and other governmental entities and membership organizations, and the impact of future firearms control and environmental legislation, any one or more of which could cause actual results to differ materially from those projected. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date made. The Company undertakes no obligation to publish revised forward-looking statements to reflect events or circumstances after the date such forward-looking statements are made or to reflect the occurrence of subsequent unanticipated events.

## **PART I**

### **ITEM 1—BUSINESS**

#### **Company Overview**

Sturm, Ruger & Company, Inc. (the “Company”) is principally engaged in the design, manufacture, and sale of firearms to domestic customers. Approximately 92% of the Company’s total sales for the year ended December 31, 2007 were from the firearms segment, and 8% were from investment castings. Export sales represent less than 6% of firearms sales. The Company’s design and manufacturing operations are located in the United States and substantially all product content is domestic.

The Company has been in the business since 1949 and was incorporated in its present form under the laws of Delaware in 1969. The Company offers products in four industry product categories – rifles, shotguns, pistols, and revolvers. The Company’s firearms are sold through a select number of independent wholesale distributors, principally to the commercial sporting market.

The Company manufactures and sells investment castings made from steel alloys for both outside customers and internal use in the firearms segment. Investment castings sold to outside customers, either directly to or through manufacturers’ representatives, represented 8% of the Company’s total sales for the year ended December 31, 2007. In July 2006, the Company announced the cessation of the titanium castings portion of its investment casting operations. This cessation of operations was completed in 2007, at which time the Company consolidated its Arizona casting operations into its New Hampshire casting operations.

For the years ended December 31, 2007, 2006, and 2005, net sales attributable to the Company's firearms operations were approximately, \$144.2 million, \$139.1 million and \$132.8 million or 92%, 83%, and 86%, respectively, of total net sales. The balance of the Company's net sales for the aforementioned periods was attributable to its investment castings operations.

#### **Firearms Products**

The Company presently manufactures firearm products, under the “Ruger” name and trademark, in the following industry categories:

##### **Rifles**

- Single-shot
- Autoloading
- Bolt-action
- Lever action

##### **Shotguns**

- Over and Under
- Side by Side

## **Pistols**

- Rimfire autoloading
- Centerfire autoloading

## **Revolvers**

- Single action
- Double action

Most firearms are available in several models based upon caliber, finish, barrel length, and other features. Many of the firearms introduced by the Company over the years have become “classics” which have retained their popularity for decades and are sought by collectors.

## **Rifles**

A rifle is a long gun with spiral grooves cut into the interior of the barrel to give the bullet a stabilizing spin after it leaves the barrel. Sales of rifles by the Company accounted for approximately \$64.9 million, \$58.4 million, and \$58.0 million, of revenues for the years 2007, 2006 and 2005, respectively.

## **Shotguns**

A shotgun is a long gun with a smooth barrel interior which fires lead or steel pellets. Sales of shotguns by the Company accounted for approximately \$3.8 million, \$5.5 million, and \$9.7 million of revenues for the years 2007, 2006 and 2005, respectively.

## **Pistols**

A pistol is a handgun in which the ammunition chamber is an integral part of the barrel and which typically is fed ammunition from a magazine contained in the grip. Sales of pistols by the Company accounted for approximately \$33.4 million, \$31.9 million, and \$32.5 million of revenues for the years 2007, 2006 and 2005, respectively.

## **Revolvers**

A revolver is a handgun that has a cylinder that holds the ammunition in a series of chambers which are successively aligned with the barrel of the gun during each firing cycle. There are two general types of revolvers, single-action and double-action. To fire a single-action revolver, the hammer is pulled back to cock the gun and align the cylinder before the trigger is pulled. To fire a double-action revolver, a single trigger pull advances the cylinder and cocks and releases the hammer. Sales of revolvers by the Company accounted for approximately \$35.6 million, \$37.6 million, and \$27.5 million of revenues for the years 2007, 2006, and 2005, respectively.

The Company also manufactures and sells accessories and replacement parts for its firearms. These sales accounted for approximately \$6.5 million, \$5.7 million, and \$5.1 million of revenues for the years 2007, 2006 and 2005, respectively.

## **Investment Casting Products**

The Company manufactures and sells investment castings made from steel alloys for both outside customers and internal use in the firearms segment. Investment castings sold to outside customers, either directly to or through manufacturers’ representatives, represented 8% of the Company’s total sales for the year ended December 31, 2007. In July 2006, the Company announced the cessation of the titanium castings portion of its investment casting operations. This cessation of operations was completed in 2007, at which time the Company consolidated its Arizona casting operations into its New Hampshire casting operations.

Net sales attributable to the Company's investment casting operations (excluding intercompany transactions) accounted for approximately \$12.3 million, \$28.5 million, and \$21.9 million, or 8%, 17%, and 14% of the Company's total net sales for 2007, 2006, and 2005, respectively.

## **Manufacturing**

### **Firearms**

The Company produces one model of pistol and all of its rifles, shotguns, and revolvers at the Newport, New Hampshire facility. All other pistols are produced at the Prescott, Arizona facility.

Many of the basic metal component parts of the firearms manufactured by the Company are produced by the Company's castings facilities through a process known as precision investment casting. See "Manufacturing-Investment Castings" for a description of the investment casting process. The Company initiated the use of this process in the production of component parts for firearms in 1953. The Company believes that the investment casting process provides greater design flexibility and results in component parts which are generally close to their ultimate shape and, therefore, require less machining than processes requiring machining a solid billet of metal to obtain a part. Through the use of investment castings, the Company endeavors to produce durable and less costly component parts for its firearms.

All assembly, inspection, and testing of firearms manufactured by the Company are performed at the Company's manufacturing facilities. Every firearm, including every chamber of every revolver manufactured by the Company, is test-fired prior to shipment.

### **Investment Castings**

To produce a product by the investment casting method, a wax model of the part is created and coated ("invested") with several layers of ceramic material. The shell is then heated to melt the interior wax which is poured off, leaving a hollow mold. To cast the desired part, molten metal is poured into the mold and allowed to cool and solidify. The mold is then broken off to reveal a near net shape cast metal part.

In July 2006, the Company announced the cessation of the titanium castings portion of its investment casting operations. This cessation of operations was completed in 2007, at which time the Company consolidated its Arizona casting operations into its New Hampshire casting operations. The Company only produces ferrous investment castings.

## **Marketing and Distribution**

### **Firearms**

The Company's firearms are primarily marketed through a network of selected Federally-licensed independent wholesale distributors who purchase the products directly from the Company. They resell to Federally-licensed retail firearms dealers who in turn resell to legally authorized end-users. All retail purchasers are subject to a point-of-sale background check by law enforcement. These end-users include sportsmen, hunters, law enforcement and other governmental organizations, and gun collectors. Each distributor carries the entire line of firearms manufactured by the Company for the commercial market. Currently, 15 distributors service the domestic commercial market, with an additional 12 distributors servicing the domestic law enforcement market and two distributors servicing the Canadian

market. Six of the Company's distributors service both the domestic commercial market and the domestic law enforcement market.

One customer accounted for 13% of firearms sales in both 2007 and 2006, and 12% and 11% of consolidated sales in 2007 and 2006, respectively. A second customer accounted for approximately 12%, 13%, and 13% of net firearms sales and 11%, 10%, and 11% of consolidated net sales in 2007, 2006, and 2005, respectively. A third customer accounted for approximately 12% of the Company's net firearms sales and 10% of consolidated net sales in 2005. A fourth customer accounted for approximately 12%, 13%, and 16% of net firearms sales in 2007, 2006, and 2005, respectively, and 11%, 11%, and 14% of consolidated net sales in 2007, 2006, and 2005, respectively.

The Company employs eight employees and one independent contractor who service these distributors and call on dealers and law enforcement agencies. Because the ultimate demand for the Company's firearms comes from end-users, rather than from the Company's distributors, the Company believes that the loss of any distributor would not have a material long-term adverse effect on the Company, but may have a material impact on the Company's financial results for a particular period. The Company considers its relationships with its distributors to be satisfactory.

The Company also exports its firearms through a network of selected commercial distributors and directly to certain foreign customers, consisting primarily of law enforcement agencies and foreign governments. Foreign sales were less than 6% of the Company's consolidated net sales for each of the past three fiscal years.

No material portion of the Company's business is subject to renegotiation of profits or termination of contracts at the election of a government purchaser.

Prior to 2006, the Company received one cancelable annual order in December from each of its distributors. Effective December 1, 2006 the Company changed the manner in which distributors order firearms, and began receiving firm, non-cancelable purchase orders on a frequent basis, with most orders for immediate delivery. As of February 1, 2008, the order backlog was \$20 million. As of February 1, 2007, order backlog was approximately \$23 million.

The Company does not consider its overall firearms business to be predictably seasonal; however, sales of many models of firearms are usually lower in the third quarter of the fiscal year.

#### Investment Castings

The investment casting segment's principal markets are commercial, sporting goods, and military. Sales are made directly to customers or through manufacturers' representatives. The Company produces various products for a number of customers in a variety of industries, including over 20 firearms and firearms component manufacturers. The investment castings segment provides castings for the Company's firearms segment.

The Company continues to evaluate the viability and profitability of the commercial castings market. The Company significantly increased prices to most external customers in the second half of the 2007, seeking to improve margins and free up available capacity for additional internal use. Certain customers accepted the price increases while others moved their business away from the Company as anticipated.

## **Competition**

### **Firearms**

Competition in the firearms industry is intense and comes from both foreign and domestic manufacturers. While some of these competitors concentrate on a single industry product category, such as rifles or pistols, several competitors manufacture products in the same four industry categories as the Company (rifles, shotguns, pistols, and revolvers). Some of these competitors are subsidiaries of larger corporations than the Company with substantially greater financial resources than the Company, which could affect the Company's ability to compete. The principal methods of competition in the industry are product innovation, quality, availability, and price. The Company believes that it can compete effectively with all of its present competitors.

### **Investment Castings**

There are a large number of investment castings manufacturers, both domestic and foreign, with which the Company competes. Competition varies based on the type of investment castings products and the end-use of the product (commercial, sporting goods, or military). Many of these competitors are larger corporations than the Company with substantially greater financial resources than the Company, which could affect the Company's ability to compete with these competitors. The principal methods of competition in the industry are quality, price, and production lead time. The Company believes that it can compete effectively with its present domestic competitors. However, it is unknown if the Company can compete with foreign competitors in the long-term.

## **Employees**

As of February 1, 2008, the Company employed approximately 1,100 full-time employees of which approximately 56% had at least ten years of service with the Company.

None of the Company's employees are subject to a collective bargaining agreement. The Company has never experienced a strike during its history and believes its employee relations are satisfactory.

## **Research and Development**

In 2007, 2006, and 2005, the Company spent approximately \$0.7 million, \$0.6 million, and \$0.8 million, respectively, on research activities relating to the development of new products and the improvement of existing products. As of February 15, 2008, the Company had approximately 10 employees whose primary responsibilities were research and development activities.

## **Patents and Trademarks**

The Company owns various United States and foreign patents and trademarks which have been secured over a period of years and which expire at various times. It is the policy of the Company to apply for patents and trademarks whenever new products or processes deemed commercially valuable are developed or marketed by the Company. However, none of these patents and trademarks are considered to be basic to any important product or manufacturing process of the Company and, although the Company deems its patents and trademarks to be of value, it does not consider its business materially dependent on patent or trademark protection.



## **Environmental Matters**

The Company is committed to achieving high standards of environmental quality and product safety, and strives to provide a safe and healthy workplace for its employees and others in the communities in which it operates. The Company has programs in place that monitor compliance with various environmental regulations. However, in the normal course of its manufacturing operations the Company is subject to occasional governmental proceedings and orders pertaining to waste disposal, air emissions, and water discharges into the environment. These regulations are integrated into the Company's manufacturing, assembly, and testing processes. The Company believes that it is generally in compliance with applicable environmental regulations and the outcome of any environmental proceedings and orders will not have a material effect on the financial position of the Company, but could have a material impact on the financial results for a particular period.

## **Executive Officers of the Company**

Set forth below are the names, ages, and positions of the executive officers of the Company. Officers serve at the discretion of the Board of Directors of the Company.

| <u>Name</u>           | <u>Age</u> | <u>Position With Company</u>  |
|-----------------------|------------|---|
| Michael O. Fifer      | 50         | Chief Executive Officer   |
| Stephen L. Sanetti    | 58         | Vice Chairman of the Board of Directors, President, and General Counsel |
| Thomas A. Dineen      | 39         | Vice President, Treasurer and Chief Financial Officer                   |
| Christopher J. Killoy | 49         | Vice President of Sales and Marketing                                   |
| Robert R. Stutler     | 64         | Vice President of Prescott Operations (Retired 2/15/2008)               |
| Mark T. Lang          | 51         | Group Vice President  |
| Thomas P. Sullivan    | 47         | Vice President of Newport Operations                                    |
| Leslie M. Gasper      | 54         | Corporate Secretary   |

Michael O. Fifer joined the Company as Chief Executive Officer on September 25, 2006, and was named to the Board of Directors on October 19, 2006. Prior to joining the Company, Mr. Fifer was President of the Engineered Products Division of Mueller Industries, Inc. Prior to joining Mueller Industries, Inc., Mr. Fifer was President, North American Operations, Watts Water Technologies.

Stephen L. Sanetti became President on May 6, 2003. Mr. Sanetti has served as General Counsel since 1980. Prior to May 6, 2003, Mr. Sanetti had been Vice Chairman and Senior Executive Vice President since October 24, 2000. Mr. Sanetti has been a Director since March 1, 1998. Prior to October 24, 2000, he had been Vice President, General Counsel of the Company since 1993.

Thomas A. Dineen became Vice President on May 24, 2006. Previously he served as Treasurer and Chief Financial Officer since May 6, 2003 and had been Assistant Controller since 2001. Prior to that, Mr. Dineen had served as Manager, Corporate Accounting since 1997.

Christopher J. Killoy rejoined the Company as Vice President of Sales and Marketing on November 27, 2006. Mr. Killoy originally joined the Company in 2003 as Executive Director of Sales and Marketing, and subsequently served as Vice President of Sales and Marketing from November 1, 2004 to January 25, 2005.

Robert R. Stutler retired on February 15, 2008. Mr. Stutler became Vice President of Operations for the Company's Prescott, Arizona Firearms and Foundry Divisions on March 17, 2006. Previously he served as General Manager of Prescott Operations since 2002 and General Manager of Prescott Firearms Division from 1990 to 2002. Mr. Stutler joined the Company in 1987.

Mark T. Lang joined the Company as Group Vice President on February 18, 2008. Mr. Lang will initially be responsible for management of the Prescott Firearms Division following the retirement of Mr. Stutler. Prior to joining the Company, Mr. Lang was President of the Custom Products Business at Mueller Industries, Inc. Prior to joining Mueller, Mr. Lang was the Vice President of Operations for the Automotive Division of Thomas and Betts, Inc.

Thomas P. Sullivan joined the Company as Vice President of Newport Operations for the Newport, New Hampshire Firearms and Pine Tree Castings divisions on August 14, 2006. Prior to joining the Company, Mr. Sullivan was Vice President of Lean Enterprises at IMI Norgren Ltd.

Leslie M. Gasper has been Secretary of the Company since 1994. Prior to this, she was the Administrator of the Company's pension plans, a position she held for more than five years prior thereto.

### **Where You Can Find More Information**

The Company is a reporting company and is therefore subject to the informational requirements of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"), and accordingly files its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Definitive Proxy Statements, Current Reports on Form 8-K, and other information with the Securities and Exchange Commission (the "SEC"). The public may read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. Please call the SEC at (800) SEC-0330 for further information on the Public Reference Room. As an electronic filer, the Company's public filings are maintained on the SEC's Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that website is <http://www.sec.gov>.

The Company makes its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Definitive Proxy Statements, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act accessible free of charge through the Company's Internet site after the Company has electronically filed such material with, or furnished it to, the SEC. The address of that website is <http://www.ruger.com>. However, such reports may not be accessible through the Company's website as promptly as they are accessible on the SEC's website.

Additionally, the Company's corporate governance materials, including its Corporate Governance Guidelines; the charters of the Audit, Compensation, and Nominating and Corporate Governance committees; and the Code of Business Conduct and Ethics may also be found under the "Stockholder Relations" section of the Company's Internet site at [www.ruger.com](http://www.ruger.com). A copy of the foregoing corporate governance materials are available upon written request of the Corporate Secretary at Sturm, Ruger & Company, Inc., Lacey Place, Southport, Connecticut 06890.

## **ITEM 1A—RISK FACTORS**

In evaluating the Company's business, the following risk factors, as well as other information in this report, should be carefully considered.

### **Firearms Legislation**

*(The following disclosures within "Firearms Legislation" are identical to the disclosures within "Firearms Legislation" in Item 7-Management's Discussion and Analysis of Financial Condition and Results of Operations.)*

The sale, purchase, ownership, and use of firearms are subject to thousands of federal, state and local governmental regulations. The basic federal laws are the National Firearms Act, the Federal Firearms Act, and the Gun Control Act of 1968. These laws generally prohibit the private ownership of fully automatic weapons and place certain restrictions on the interstate sale of firearms unless certain licenses are obtained. The Company does not manufacture fully automatic weapons, other than for the law enforcement market, and holds all necessary licenses under these federal laws. From time to time, congressional committees review proposed bills relating to the regulation of firearms. These proposed bills generally seek either to restrict or ban the sale and, in some cases, the ownership of various types of firearms. Several states currently have laws in effect similar to the aforementioned legislation.

Until November 30, 1998, the "Brady Law" mandated a nationwide five-day waiting period and background check prior to the purchase of a handgun. As of November 30, 1998, the National Instant Check System, which applies to both handguns and long guns, replaced the five-day waiting period. The Company believes that the "Brady Law" and the National Instant Check System have not had a significant effect on the Company's sales of firearms, nor does it anticipate any impact on sales in the future. On September 13, 1994, the "Crime Bill" banned so-called "assault weapons." All the Company's then-manufactured commercially-sold long guns were exempted by name as "legitimate sporting firearms." This ban expired by operation of law on September 13, 2004. The Company remains strongly opposed to laws which would restrict the rights of law-abiding citizens to lawfully acquire firearms. The Company believes that the lawful private ownership of firearms is guaranteed by the Second Amendment to the United States Constitution and that the widespread private ownership of firearms in the United States will continue. However, there can be no assurance that the regulation of firearms will not become more restrictive in the future and that any such restriction would not have a material adverse effect on the business of the Company.

## **Firearms Litigation**

*(The following disclosures within “Firearms Litigation” are identical to the disclosures within “Firearms Litigation” in Item 7-Management’s Discussion and Analysis of Financial Condition and Results of Operations and Note 6 of the notes to the financial statements-Contingent Liabilities.)*

As of December 31, 2007, the Company is a defendant in approximately 5 lawsuits involving its products and is aware of certain other such claims. These lawsuits and claims fall into two categories:

- (i) those that claim damages from the Company related to allegedly defective product design which stem from a specific incident. Pending lawsuits and claims are based principally on the theory of “strict liability” but also may be based on negligence, breach of warranty, and other legal theories; and
- (ii) those brought by cities or other governmental entities, and individuals against firearms manufacturers, distributors and dealers seeking to recover damages allegedly arising out of the misuse of firearms by third parties in the commission of homicides, suicides and other shootings involving juveniles and adults. The complaints by municipalities seek damages, among other things, for the costs of medical care, police and emergency services, public health services, and the maintenance of courts, prisons, and other services. In certain instances, the plaintiffs seek to recover for decreases in property values and loss of business within the city due to criminal violence. In addition, nuisance abatement and/or injunctive relief is sought to change the design, manufacture, marketing and distribution practices of the various defendants. These suits allege, among other claims, strict liability or negligence in the design of products, public nuisance, negligent entrustment, negligent distribution, deceptive or fraudulent advertising, violation of consumer protection statutes and conspiracy or concert of action theories. Most of these cases do not allege a specific injury to a specific individual as a result of the misuse or use of any of the Company’s products.

The Company has expended significant amounts of financial resources and management time in connection with product liability litigation. Management believes that, in every case involving firearms, the allegations are unfounded, and that the shootings and any results therefrom were due to negligence or misuse of the firearms by third-parties or the claimant, and that there should be no recovery against the Company. Defenses further exist to the suits brought by governmental entities based, among other reasons, on established state law precluding recovery for essential government services, the remoteness of the claims, the types of damages sought to be recovered, and limitations on the extraterritorial authority which may be exerted by a city, municipality, county or state under state and federal law, including State and Federal Constitutions.

The only case against the Company alleging liability for criminal shootings by third-parties to ever be permitted to go before a constitutional jury, Hamilton, et al. v. Accu-tek, et al., resulted in a defense verdict in favor of the Company on February 11, 1999. In that case, numerous firearms manufacturers and distributors had been sued, alleging damages as a result of alleged negligent sales practices and “industry-wide” liability. The Company and its marketing and distribution practices were exonerated from any claims of negligence in each of the seven cases decided by the jury. In subsequent proceedings involving other defendants, the New York Court of Appeals as a matter of law confirmed that 1) no legal duty existed under the circumstances to prevent or investigate criminal misuses of a manufacturer’s lawfully made products; and 2) liability of firearms manufacturers could not be apportioned under a market share theory. More recently, the New York Court of Appeals on October 21,

2003 declined to hear the appeal from the decision of the New York Supreme Court, Appellate Division, affirming the dismissal of New York Attorney General Eliot Spitzer's public nuisance suit against the Company and other manufacturers and distributors of firearms. In its decision, the Appellate Division relied heavily on Hamilton in concluding that it was "legally inappropriate," "impractical," "unrealistic" and "unfair" to attempt to hold firearms manufacturers responsible under theories of public nuisance for the criminal acts of others.

Of the lawsuits brought by municipalities, counties or a state Attorney General, twenty have been concluded: Atlanta – dismissal by intermediate Appellate Court, no further appeal; Bridgeport – dismissal affirmed by Connecticut Supreme Court; County of Camden – dismissal affirmed by U.S. Third Circuit Court of Appeals; Miami – dismissal affirmed by intermediate appellate court, Florida Supreme Court declined review; New Orleans – dismissed by Louisiana Supreme Court, United States Supreme Court declined review; Philadelphia – U.S. Third Circuit Court of Appeals affirmed dismissal, no further appeal; Wilmington – dismissed by trial court, no appeal; Boston – voluntary dismissal with prejudice by the City at the close of fact discovery; Cincinnati – voluntarily withdrawn after a unanimous vote of the city council; Detroit – dismissed by Michigan Court of Appeals, no appeal; Wayne County – dismissed by Michigan Court of Appeals, no appeal; New York State – Court of Appeals denied plaintiff's petition for leave to appeal the Intermediate Appellate Court's dismissal, no further appeal; Newark – Superior Court of New Jersey Law Division for Essex County dismissed the case with prejudice; City of Camden – dismissed on July 7, 2003, not reopened; Jersey City – voluntarily dismissed and not re-filed; St. Louis – Missouri Supreme Court denied plaintiffs' motion to appeal Missouri Appellate Court's affirmation of dismissal; Chicago – Illinois Supreme Court affirmed trial court's dismissal; and Los Angeles City, Los Angeles County, San Francisco – Appellate Court affirmed summary judgment in favor of defendants, no further appeal; and Cleveland – dismissed on January 24, 2006 for lack of prosecution.

The dismissal of the Washington, D.C. municipal lawsuit was sustained on appeal, but individual plaintiffs were permitted to proceed to discovery and attempt to identify the manufacturers of the firearms used in their shootings as "machine guns" under the city's "strict liability" law. On April 21, 2005, the D.C. Court of Appeals, in an *en banc* hearing, unanimously dismissed all negligence and public nuisance claims, but let stand individual claims based upon a Washington, D.C. act imposing "strict liability" for manufacturers of "machine guns." Based on present information, none of the Company's products has been identified with any of the criminal assaults which form the basis of the individual claims. The writ of certiorari to the United States Supreme Court regarding the constitutionality of the Washington, D.C. act was denied and the case was remanded to the trial court for further proceedings. The defendants subsequently moved to dismiss the case based upon the Protection of Lawful Commerce in Arms Act, which motion was granted on May 22, 2006. The individual plaintiffs and the District of Columbia, which has subrogation claims in regard to the individual plaintiffs, appealed. On January 10, 2008, the District of Columbia Court of Appeals unanimously upheld the dismissal. Plaintiffs have until February 25, 2008, to move for rehearing *en banc*.

The Indiana Court of Appeals affirmed the dismissal of the Gary case by the trial court, but the Indiana Supreme Court reversed this dismissal and remanded the case for discovery proceedings on December 23, 2003. Gary is scheduled to begin trial in 2009. The defendants filed a motion to dismiss pursuant to the Protection of Lawful Commerce in Arms Act ("PLCAA"). The state court judge held the PLCAA unconstitutional and the defendants filed a motion with the Indiana Court of Appeals asking it to accept interlocutory appeal on the issue, which appeal was accepted on February 5, 2007. On October 29, 2007, the Indiana Appellate Court affirmed, holding that the PLCAA does not apply to the City's

claims. A petition for rehearing was filed in the Appellate Court and denied on January 9, 2008. A Petition to Transfer the appeal to the Supreme Court of Indiana was filed on February 7, 2008.

In the previously reported New York City municipal case, the defendants moved to dismiss the suit pursuant to the Protection of Lawful Commerce in Arms Act. The trial judge found the Act to be constitutional but denied the defendants' motion to dismiss the case, stating that the Act was not applicable to the suit. The defendants were given leave to appeal and in fact have appealed the decision to the U.S. Court of Appeals for the Second Circuit. That appeal remains pending.

In the NAACP case, on May 14, 2003, an advisory jury returned a verdict rejecting the NAACP's claims. On July 21, 2003, Judge Jack B. Weinstein entered an order dismissing the NAACP lawsuit, but this order contained lengthy dicta which defendants believe are contrary to law and fact. Appeals by both sides were filed, but plaintiffs withdrew their appeal. On August 3, 2004, the United States Court of Appeals for the Second Circuit granted the NAACP's motion to dismiss the defendants' appeal of Judge Weinstein's order denying defendants' motion to strike his dicta made in his order dismissing the NAACP's case, and the defendants' motion for summary disposition was denied as moot. The ruling of the Second Circuit effectively confirmed the decision in favor of defendants and brought this matter to a conclusion.

Legislation has been passed in approximately 34 states precluding suits of the type brought by the municipalities mentioned above. On the Federal level, the "Protection of Lawful Commerce in Arms Act" was signed by President Bush on October 26, 2005. The Act requires dismissal of suits against manufacturers arising out of the lawful sale of their products for harm resulting from the criminal or unlawful misuse of a firearm by a third party. The Company is pursuing dismissal of each action involving such claims, including the municipal cases described above. The Company was voluntarily dismissed with prejudice on March 23, 2007 from the previously reported Arnold case. The matter was thus concluded with no payment by the Company.

Punitive damages, as well as compensatory damages, are demanded in certain of the lawsuits and claims. Aggregate claimed amounts presently exceed product liability accruals and applicable insurance coverage. For claims made after July 10, 2000, coverage is provided on an annual basis for losses exceeding \$5 million per claim, or an aggregate maximum loss of \$10 million annually, except for certain new claims which might be brought by governments or municipalities after July 10, 2000, which are excluded from coverage.

Product liability claim payments are made when appropriate if, as, and when claimants and the Company reach agreement upon an amount to finally resolve all claims. Legal costs are paid as the lawsuits and claims develop, the timing of which may vary greatly from case to case. A time schedule cannot be determined in advance with any reliability concerning when payments will be made in any given case.

Provision is made for product liability claims based upon many factors related to the severity of the alleged injury and potential liability exposure, based upon prior claim experience. Because our experience in defending these lawsuits and claims is that unfavorable outcomes are typically not probable or estimable, only in rare cases is an accrual established for such costs. In most cases, an accrual is established only for estimated legal defense costs. Product liability accruals are periodically reviewed to reflect then-current estimates of possible liabilities and expenses incurred to date and reasonably anticipated in the future. Threatened product liability claims are reflected in our product

liability accrual on the same basis as actual claims; i.e., an accrual is made for reasonably anticipated possible liability and claims-handling expenses on an ongoing basis.

A range of reasonably possible loss relating to unfavorable outcomes cannot be made. However, in product liability cases in which a dollar amount of damages is claimed, the amount of damages claimed, which totaled \$5 million and \$0 at December 31, 2007 and 2006, respectively, are set forth as an indication of possible maximum liability that the Company might be required to incur in these cases (regardless of the likelihood or reasonable probability of any or all of this amount being awarded to claimants) as a result of adverse judgments that are sustained on appeal.

As of December 31, 2007 and 2006, the Company was a defendant in 5 and 4 lawsuits, respectively, involving its products and is aware of other such claims. During the year ended December 31, 2007 and 2006, respectively, 2 and 2 claims were filed against the Company, 1 and 2 claims were dismissed, and 0 and 2 claims were settled. The average cost per settled claim was \$47,000 in 2006.

During the years ended December 31, 2007 and 2006, the Company incurred product liability expense of \$1.7 million and \$2.5 million, respectively, which includes the cost of outside legal fees, insurance, and other expenses incurred in the management and defense of product liability matters.

The Company management monitors the status of known claims and the product liability accrual, which includes amounts for asserted and unasserted claims. While it is not possible to forecast the outcome of litigation or the timing of costs, in the opinion of management, after consultation with special and corporate counsel, it is not probable and is unlikely that litigation, including punitive damage claims, will have a material adverse effect on the financial position of the Company, but may have a material impact on the Company's financial results for a particular period.

The Company has reported all cases instituted against it through September 30, 2007 and the results of those cases, where terminated, to the S.E.C. on its previous Form 10-K and 10-Q reports, to which reference is hereby made.

**Balance Sheet Rollforward for Product Liability Reserve**  
(Dollars in thousands)

|      | Balance<br>Beginning<br>of Year (a) | Accrued<br>Legal<br>Expense<br>(b) | Cash Payments     |                     |                       |                   | Balance<br>End of<br>Year (a) |
|------|-------------------------------------|------------------------------------|-------------------|---------------------|-----------------------|-------------------|-------------------------------|
|      |                                     |                                    | Legal Fees<br>(c) | Settlement<br>s (d) | Insurance<br>Premiums | Admin.<br>Expense |                               |
| 2005 | \$3,132                             | \$2,514                            | \$(2,935)         | (515)               | N/A                   | N/A               | \$2,196                       |
| 2006 | 2,196                               | 688                                | (1,000)           | (143)               | N/A                   | N/A               | 1,741                         |
| 2007 | 1,741                               | 639                                | (447)             | -                   | N/A                   | N/A               | 1,933                         |

## Income Statement Detail for Product Liability Expense

(Dollars in thousands)

|      | Accrued<br>Legal<br>Expense<br>(b) | Insurance<br>Premium<br>Expense<br>(e) | Admin.<br>Expense<br>(f) | Total<br>Product<br>Liability<br>Expense |
|------|------------------------------------|--|--------------------------|--|
| 2005 | \$2,514                            | \$1,338                                | \$1,041                  | \$4,893                                  |
| 2006 | 688                                | 1,141                                  | 691                      | 2,520                                    |
| 2007 | 639                                | 748                                    | 299                      | 1,686                                    |

### Notes

- (a) The beginning and ending liability balances represent accrued legal fees only. Settlements and administrative costs are expensed as incurred. Only in rare instances is an accrual established for settlements.
- (b) The expense accrued in the liability is for legal fees only.
- (c) Legal fees represent payments to outside counsel related to product liability matters.
- (d) Settlements represent payments made to plaintiffs or allegedly injured parties in exchange for a full and complete release of liability.
- (e) Insurance expense represents the cost of insurance premiums.
- (f) Administrative expense represents personnel related and travel expenses of Company employees and firearm experts related to the management and monitoring of product liability matters.

There were no insurance recoveries during any of the above years.

### Environmental

The Company is subject to numerous federal, state and local laws and governmental regulations and related state laws. These laws generally relate to potential obligations to remove or mitigate the environmental effects of the disposal or release of certain pollutants at the Company's manufacturing facilities and at third-party or formerly owned sites at which contaminants generated by the Company may be located. This requires the Company to make capital and other expenses.

The Company is committed to achieving high standards of environmental quality and product safety, and strives to provide a safe and healthy workplace for its employees and others in the communities in which it operates. In an effort to comply with federal and state laws and regulations, the Company has programs in place that monitor compliance with various environmental regulations. However, in the normal course of its operations, the Company is subject to occasional governmental proceedings and orders pertaining to waste disposal, air emissions, and water discharges into the environment.



The Company believes that it is generally in compliance with applicable environmental regulations. However, the Company cannot assure that the outcome of any environmental proceedings and orders will not have a material adverse effect on the business.

**Reliance on Two Facilities**

The Newport, New Hampshire and Prescott, Arizona facilities are critical to the Company’s success. These facilities house the Company’s principal production, research, development, engineering, design, and shipping. Any event that causes a disruption of the operation of either of these facilities for even a relatively short period of time might have a material adverse affect on the Company’s ability to produce and ship products and to provide service to its customers.

**Availability of Raw Materials**

Third parties supply the Company with various raw materials for its firearms and castings, such as fabricated steel components, walnut, birch, beech, maple and laminated lumber for rifle and shotgun stocks, wax, ceramic material, metal alloys, various synthetic products and other component parts. There is a limited supply of these materials in the marketplace at any given time, which can cause the purchase prices to vary based upon numerous market factors. The Company believes that it has adequate quantities of raw materials in inventory to provide ample time to locate and obtain additional items at then-current market cost without interruption of its manufacturing operations. However, if market conditions result in a significant prolonged inflation of certain prices or if adequate quantities of raw materials can not be obtained, the Company’s manufacturing processes could be interrupted and the Company’s financial condition or results of operations could be materially adversely affected.

**ITEM 1B—UNRESOLVED STAFF COMMENTS**

None

**ITEM 2—PROPERTIES**

The Company’s manufacturing operations are carried out at two facilities. The following table sets forth certain information regarding each of these facilities:

|                        | Approximate<br>Aggregate<br>Usable<br>Square Feet | Status | Segment           |
|------------------------|---|--------|-------------------|
| Newport, New Hampshire | 350,000   | Owned  | Firearms/Castings |
| Prescott, Arizona      | 230,000   | Leased | Firearms          |

Each facility contains enclosed ranges for testing firearms and also contains modern tool room facilities. The lease of the Prescott facility provides for rental payments, which are approximately equivalent to estimated rates for real property taxes. The Company consolidated its casting operations in its Newport, New Hampshire foundry in 2007.

The Company has three other facilities that were not used in its manufacturing operations in 2007:

|   | Approximate<br>Aggregate<br>Usable<br>Square Feet | Status | Segment      |
|---|---|--------|--------------|
| Southport, Connecticut<br>(Station Street property) | 5,000   | Owned  | Not Utilized |
| Southport, Connecticut<br>(Lacey Place property)    | 25,000  | Owned  | Corporate    |
| Newport, New Hampshire<br>(Dorr Woolen Building)    | 300,000   | Owned  | Firearms (a) |

- (a) In 2005, the Company relocated its firearms shipping department into a portion of the the Dorr Woolen Building. In 2006, certain of the Company's sales department personnel were moved into the same facility.

There are no mortgages or any other major encumbrance on any of the real estate owned by the Company. The Company sold some of its non-manufacturing real property assets in 2007. The three non-manufacturing facilities identified above are listed for sale.

The Company's principal executive offices are located in Southport, Connecticut. The Company believes that its existing facilities are suitable and adequate for its present purposes.

### **ITEM 3—LEGAL PROCEEDINGS**

The nature of the legal proceedings against the Company is discussed at Note 6 of the notes to the financial statements in this Annual Report on Form 10-K report, which is incorporated herein by reference.

The Company has reported all cases instituted against it through September 30, 2007, and the results of those cases, where terminated, to the S.E.C. on its previous Form 10-Q and 10-K reports, to which reference is hereby made.

No cases were formally instituted against the Company during the three months ending December 31, 2007.

During the three months ending December 31, 2007, no previously reported cases were settled.

For a description of all pending lawsuits against the Company through September 30, 2007, reference is made to the discussion under the caption "Item 1. LEGAL PROCEEDINGS" of the Company's Quarterly Reports on Form 10-Q for the quarters ended September 30, 1999, March 31 and September 30, 2000, and June 30, 2007.

### **ITEM 4—SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

## PART II

### ITEM 5—MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company's Common Stock is traded on the New York Stock Exchange under the symbol "RGR." At February 1, 2008, the Company had 1,769 stockholders of record.

The following table sets forth, for the periods indicated, the high and low sales prices for the Common Stock as reported on the New York Stock Exchange and dividends paid on Common Stock.

|                | High    | Low     | Dividends<br>Per Share |
|----------------|---------|---------|------------------------|
| 2006:          |         |         |                        |
| First Quarter  | \$ 8.03 | \$ 6.75 | -                      |
| Second Quarter | 7.78    | 5.56    | -                      |
| Third Quarter  | 7.85    | 5.65    | -                      |
| Fourth Quarter | 10.78   | 7.74    | -                      |
| 2007:          |         |         |                        |
| First Quarter  | \$13.27 | \$8.91  | -                      |
| Second Quarter | 15.49   | 11.77   | -                      |
| Third Quarter  | 20.94   | 13.86   | -                      |
| Fourth Quarter | 18.35   | 7.22    | -                      |

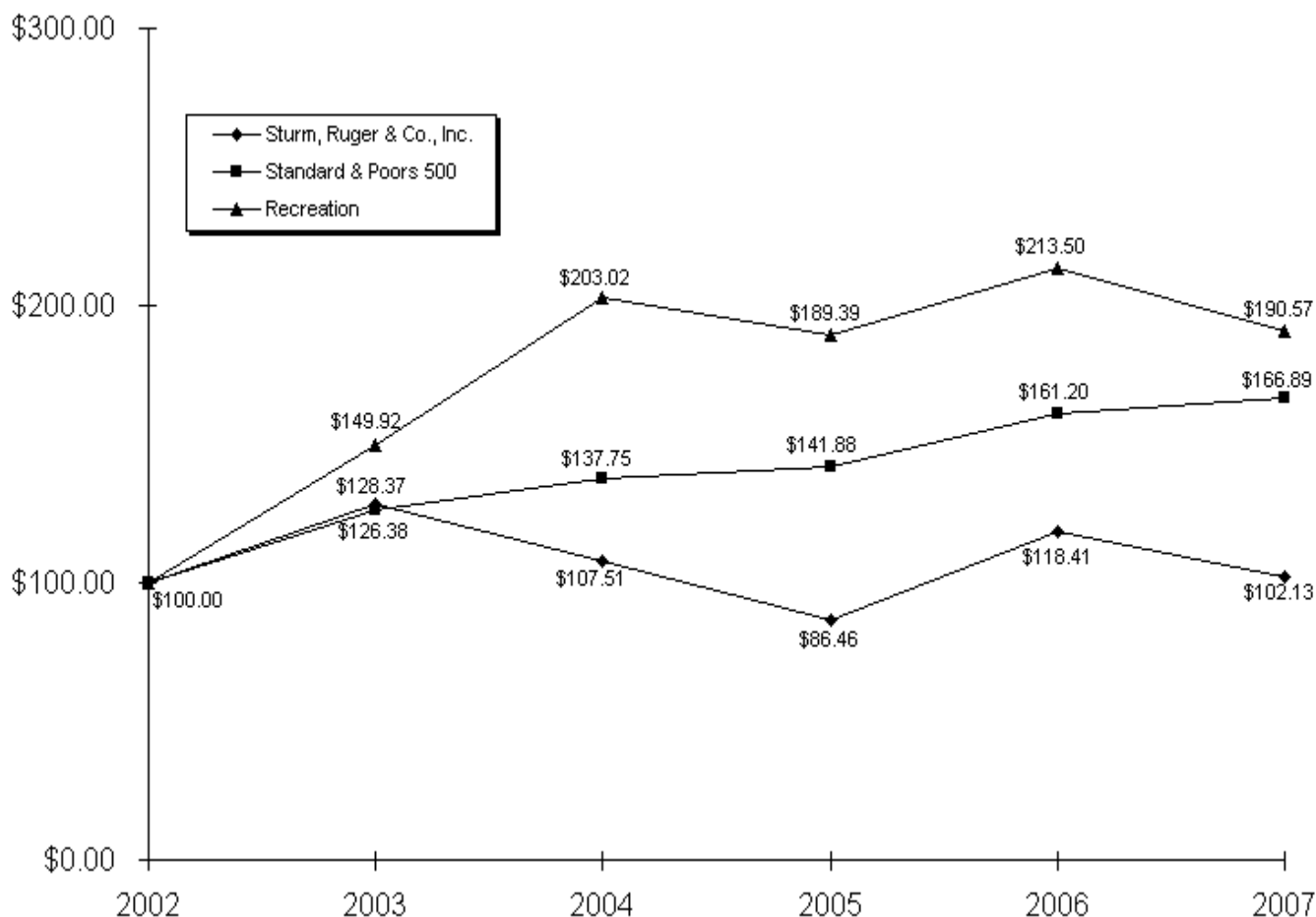
#### Issuer Repurchase of Equity Securities

| Dates                            | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>Per Share | Total Number<br>of Shares<br>Purchased<br>Under the<br>Program | Approximate<br>Dollar Value of<br>Shares that may<br>yet be<br>Purchased<br>Under the<br>Program |
|----------------------------------|---|------------------------------------|--|--|
| October 1 –<br>December 31, 2007 | 2,216,000                                 | \$ 8.99                            | 2,216,000  | \$ 0 (Note 1)  |
| Total                            | 2,216,000                                 | \$ 8.99                            | 2,216,000  | \$ 0   |

- (1) In the first quarter of 2007, the Board of Directors authorized a \$20 million stock repurchase program. Through December 31, 2007 all share repurchases were open market purchases.

On September 26, 2006, the Company repurchased 4,272,000 shares of its common stock, representing 15.9% of the outstanding shares, from entities controlled by members of the Ruger family at a price of \$5.90 per share. These purchases were made with cash held by the Company and no debt was incurred.

**Comparison of Five-Year Cumulative Total Return\***  
**Sturm, Ruger & Company, Inc., Standard & Poor's 500 And**  
**Value Line Recreation Index**  
**(Performance Results Through 12/31/07)**



\*Cumulative total return assumes reinvestment of dividends.

**Source: Value Line, Inc.**

Factual material is obtained from sources believed to be reliable, but the publisher is not responsible for any errors or omissions contained herein.

|                              | 2002   | 2003   | 2004   | 2005   | 2006   | 2007   |
|------------------------------|--------|--------|--------|--------|--------|--------|
| Sturm, Ruger & Company, Inc. | 100.00 | 128.37 | 107.51 | 86.46  | 118.41 | 102.13 |
| Standard & Poor's 500        | 100.00 | 126.38 | 137.75 | 141.88 | 161.20 | 166.89 |
| Recreation                   | 100.00 | 149.92 | 203.02 | 189.39 | 213.50 | 190.57 |

## Securities Authorized for Issuance Under Equity Compensation Plans

The following table provides information regarding compensation plans under which equity securities of the Company are authorized for issuance as of December 31, 2007:

| <b>Equity Compensation Plan Information</b>                       |  |  |  |
|---|--|--|--|
| <b>Plan category</b>  | <b>Number of securities to be issued upon exercise of outstanding options, warrants and rights</b> | <b>Weighted-average exercise price of outstanding options, warrants and rights</b> | <b>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))</b> |
|   | <b>(a)</b>   | <b>(b)</b>   | <b>(c)</b>   |
| <b>Equity compensation plans approved by security holders</b>     |  |  |  |
| 1998 Stock Incentive Plan   | 600,000  | \$7.77 per share   | -  |
| 2001 Stock Option Plan for Non-Employee Directors                 | 180,000  | \$8.75 per share   | -  |
| 2007 Stock Incentive Plan   | 311,250  | \$13.06 per share  | 2,238,750  |
| <b>Equity compensation plans not approved by security holders</b> |  |  |  |
| None.   |  |  |  |
| <b>Total</b>  | 1,091,250  | \$9.44 per share   | 2,238,750  |

## ITEM 6—SELECTED FINANCIAL DATA

*(Dollars in thousands, except per share data)*

|                                      | December 31, |           |           |           |           |
|--------------------------------------|--------------|-----------|-----------|-----------|-----------|
|                                      | 2007         | 2006      | 2005      | 2004      | 2003      |
| Net firearms sales                   | \$144,222    | \$139,110 | \$132,805 | \$124,924 | \$130,558 |
| Net castings sales                   | 12,263       | 28,510    | 21,917    | 20,700    | 17,359    |
| Total net sales                      | 156,485      | 167,620   | 154,722   | 145,624   | 147,917   |
| Cost of products sold                | 117,186      | 139,610   | 124,826   | 115,725   | 113,189   |
| Gross profit                         | 39,299       | 28,010    | 29,896    | 29,899    | 34,728    |
| Income before income taxes           | 16,659       | 1,843     | 1,442     | 8,051     | 20,641    |
| Income taxes                         | 6,330        | 739       | 578       | 3,228     | 8,277     |
| Net income                           | \$10,329     | 1,104     | 864       | 4,823     | 12,364    |
| Basic and diluted earnings per share | 0.46         | 0.04      | 0.03      | 0.18      | 0.46      |
| Cash dividends per share             | \$0.00       | \$0.00    | \$0.30    | \$0.60    | \$0.80    |

|                                  | December 31, |            |            |            |            |
|----------------------------------|--------------|------------|------------|------------|------------|
|                                  | 2007         | 2006       | 2005       | 2004       | 2003       |
| Working capital                  | \$53,264     | \$ 60,522  | \$ 83,522  | \$ 90,947  | \$102,715  |
| Total assets                     | 101,882      | 117,066    | 139,639    | 147,460    | 162,873    |
| Total stockholders' equity       | 76,069       | 87,326     | 111,578    | 120,687    | 133,640    |
| Book value per share             | \$ 3.570     | \$ 3.86    | \$ 4.15    | \$ 4.48    | \$ 4.97    |
| Return on stockholders' equity   | 12.6%        | 1.3%       | 0.8%       | 4.0%       | 9.3%       |
| Current ratio                    | 3.6 to 1     | 3.8 to 1   | 5.5 to 1   | 5.7 to 1   | 5.7 to 1   |
| Common shares outstanding        | 20,571,800   | 22,638,700 | 26,910,700 | 26,910,700 | 26,910,700 |
| Number of stockholders of record | 1,769        | 1,851      | 1,922      | 1,977      | 2,036      |
| Number of employees              | 1,154        | 1,108      | 1,250      | 1,291      | 1,251      |

## ITEM 7—MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Company Overview

Sturm, Ruger & Company, Inc. (the "Company") is principally engaged in the design, manufacture, and sale of firearms to domestic customers. Approximately 92% of the Company's total sales for the year ended December 31, 2007 were from the firearms segment, and 8% were from investment castings. Export sales represent less than 6% of firearms sales. The Company's design and manufacturing operations are located in the United States and substantially all product content is domestic. The Company's firearms are sold through a select number of independent wholesale distributors principally to the commercial sporting market.

The Company manufactures and sells investment castings made from steel alloys for both outside customers and internal use in the firearms segment. Investment castings sold to outside customers, either directly to or through manufacturers' representatives, represented 8% of the Company's total sales for the year ended December 31, 2007. In July 2006, the Company announced the cessation of the titanium castings portion of its investment casting operations. This cessation of operations was

completed in 2007, at which time the Company consolidated its Arizona casting operations into its New Hampshire casting operations.

Because most of the Company's competitors are not subject to public filing requirements and industry-wide data is generally not available in a timely manner, the Company is unable to compare its performance to other companies or specific current industry trends. Instead, the Company measures itself against its own historical results.

The Company does not consider its overall firearms business to be predictably seasonal; however, sales of many models of firearms are usually lower in the third quarter of the year.

### **Results of Operations**

*Year ended December 31, 2007, as compared to year ended December 31, 2006:*

#### Summary Unit Data

Firearms unit data for orders, production, shipments and ending inventory, and castings setups (a measure of foundry production) are as follows:

|   | 2007    | 2006     | 2005     |
|---|---------|----------|----------|
| Units Ordered                             | 485,000 | Note (1) | Note (1) |
| Units Produced                            | 464,919 | 419,834  | 414,600  |
| Units Shipped                             | 481,832 | 475,858  | 460,243  |
| Units – Company Inventory                 | 38,309  | 55,222   | 111,246  |
| Units – Distributor Inventory<br>(Note 2) | 62,018  | 57,126   | 70,498   |
| Units on Backorder                        | 36,514  | Note (1) | Note (1) |
| Castings Setups                           | 156,133 | 169,077  | 174,443  |

Note 1: Prior to 2006, the Company received one cancelable annual firearms order in December from each of its distributors. Effective December 1, 2006, the Company changed the manner in which distributors order firearms, and began receiving firm, non-cancelable purchase orders on a frequent basis, with most orders for immediate delivery. Because of this change, comparable data for orders received and units on backorder for prior periods is not meaningful.

Note 2: Distributor ending inventory as provided by the Company's distributors.

### Orders Received

The Company saw unusually high bookings during the 1<sup>st</sup> quarter of 2007 and then unusually low bookings during the 3<sup>rd</sup> quarter of 2007. Bookings picked up again during the 4<sup>th</sup> quarter, gaining strength during the quarter. The Company's distributors indicated anecdotally that this order pattern was in line with what the overall industry experienced during 2007. This order pattern in 2007 was more volatile than the modest seasonality typically encountered in other years. Certain product lines were on backorder throughout the year, including new product introductions and low-volume products that were not in regular production throughout the year. The Company initiated sales promotions during the 3<sup>rd</sup> and 4<sup>th</sup> quarters of the year to encourage demand for those product lines where manufacturing capacity exceeded current demand.

### Production

Throughout 2007, the Company continued to work on the transition from large-scale batch production to lean manufacturing, with an emphasis on setting up manufacturing cells that facilitate flow production and pull systems. To date, the Company has converted over 70% of its batch manufacturing processes to single-piece or small-batch flow cells. In addition to continuing to set up flow cells, the next phase of the lean transition includes developing pull systems to link the assembly cells, component manufacturing cells, and parts suppliers.

In the first half of 2007, unit shipments exceeded production and there was a significant reduction in finished goods inventory. There was also a significant reduction in work-in-process inventory in the first half of 2007 as available work-in-process inventory allowed the Company to produce more units than its staffing and manufacturing processes would have otherwise allowed.

As a result of reducing gross inventory by \$28.3 million in the second half of 2006 and by \$26.6 million in the first half of 2007, including significant reductions in work-in-process inventory, many issues with design for manufacturability, poor machinery and tool reliability, weak manufacturing processes, long machine changeover times, and vendor supply were identified. The Company has made partial progress in addressing these issues with careful re-engineering of both our product and component designs and manufacturing processes as problems were identified, with the net result for certain product lines of significantly reduced factory throughput time, improved quality, and modestly improved productivity. The rate of product returns (from firearms in service less than 1 year) dropped by approximately 30% from the first quarter of 2007 to the fourth quarter of 2007. The Company was also able to increase unit production by approximately 10% from 2006 to 2007.

During the 2<sup>nd</sup> half of 2007, the Company slowed its rapid, wide-spread draw down of inventory and increased the foundry output to replenish component part shortages. Gross inventory was relatively unchanged during the 2<sup>nd</sup> half of 2007. Production rates started to increase late in 2007 as a result of the months of effort spent addressing manufacturing process and design-for-manufacturability issues and as a result of the increased availability of investment cast component parts. Nonetheless, the improvement process is ongoing with much work, especially engineering, still to be done to continue with the lean transition and to increase production capacity.

### Sales

Consolidated net sales were \$156.5 million in 2007. This represents a decrease of \$11.1 million or 6.6% from 2006 consolidated net sales of \$167.6 million.

Firearms segment net sales were \$144.2 million in 2007. This represents an increase of \$5.1 million or 3.7% from 2006 firearm net sales of \$139.1 million. Firearms unit shipments increased 1% in 2007 due



to increased shipments of rifles and pistols, offset by a decline in shipments of revolvers and shotguns. A modest price increase and a shift in product mix toward firearms with greater unit sales prices resulted in the greater percentage increase in sales than unit shipments.

Casting segment net sales were \$12.3 million in 2007. This represents a decrease of \$16.2 million or 57.0% from 2006 casting sales of \$28.5 million.

The casting sales decrease in 2007 primarily reflects the cessation of titanium casting operations, as previously announced by the Company in July 2006. In 2007, titanium casting sales were \$3.2 million or 26% of total casting sales compared to \$16.2 million or 56% in 2006. In addition, the Company significantly increased prices to most external customers in the second half of the 2007, seeking to improve margins and free up available capacity for additional internal use. Certain customers accepted the price increases while others moved their business away from the Company as anticipated.

#### Cost of Products Sold and Gross Margin

Consolidated cost of products sold was \$117.2 million in 2007. This represents a decrease of \$22.4 million or 16.1% from 2006 consolidated cost of products sold of \$139.6 million.

The gross margin as a percent of sales was 25.1% in 2007. This represents an increase from the 2006 gross margin of 16.7% as illustrated below:

|  | December 31,     |               |                  |              |
|--|------------------|---------------|------------------|--------------|
|  | 2007             |               | 2006             |              |
| Net sales  | \$156,485        | 100.0%        | \$167,620        | 100.0%       |
| Total cost of products sold,<br>before LIFO and overhead rate<br>adjustments to inventory and<br>product liability | <u>123,170</u>   | <u>78.7%</u>  | <u>135,881</u>   | <u>81.1%</u> |
| Performance gross margin *   | <u>33,315</u>    | <u>21.3%</u>  | <u>31,739</u>    | <u>18.9%</u> |
| LIFO and overhead rate<br>inventory adjustments and<br>product liability   | <u>(5,984)</u>   | <u>(3.8)%</u> | <u>3,729</u>     | <u>2.2%</u>  |
| Gross margin   | <u>\$ 39,299</u> | <u>25.1%</u>  | <u>\$ 28,010</u> | <u>16.7%</u> |

\* Performance Gross Margin is a measure of gross margin before taking into account the impact of LIFO and overhead rate adjustments to inventory, and before product liability expenses.

Excess and Obsolete Inventory—Prior to 2006, the Company adjusted production schedules to consume on-hand raw material and WIP inventories, regardless of customer demand for the finished goods so produced. This practice led to increased investment in inventory, and an unbalanced finished goods inventory.

Consistent with the change in the manner in which distributors order from the Company, the Company significantly changed its production scheduling philosophy from an annual production cycle to a customer-demand pull system in the fourth quarter of 2006. Under the Company's new system, production is driven solely by customer demand.

As a result of this new production philosophy, it became apparent that the Company had inventory in excess of its needs over the foreseeable future. Therefore, in 2006, the Company evaluated the adequacy of the excess and obsolescence inventory reserve and concluded that additional reserves were required to reflect the estimated recoverable value of excess inventories below LIFO carrying cost. The required reserve was estimated at \$5.5 million as of December 31, 2006.

The Company employed the same methodology and parameters in 2007, which resulted in a reserve balance as of December 31, 2007 of \$4.1 million. This reduction was principally caused by the increased impact of LIFO in 2007 as evidenced by the LIFO reserve representing 73% of gross inventories at December 31, 2007, compared to 66% at December 31, 2006.

Performance Gross Margin—In 2007, performance gross margin was \$33.3 million or 21.3% of sales. This was an increase of \$1.6 million or 5.0% from the 2006 performance gross margin of \$31.7 million or 18.9% of sales.

LIFO—In 2007, gross inventories were reduced by \$23.1 million compared to decreases in gross inventories of \$24.0 million in 2006. The 2007 inventory reduction resulted in LIFO income and decreased cost of products sold of \$9.1 million compared to LIFO income and decreased cost of products sold of \$1.2 million in 2006.

Overhead Rate Change—In 2007, the change in inventory value resulting from the change in the overhead rate used to absorb overhead expenses into inventory was a decrease of \$1.4 million. This reduction in inventory value resulted in an increase to cost of products sold.

In 2006, the change in inventory value resulting from the change in the overhead rate used to absorb overhead expenses into inventory was a decrease of \$2.9 million. This reduction in inventory value resulted in an increase to cost of products sold.

Product Liability—During the years ended December 31, 2007 and 2006, the Company incurred product liability expense of \$1.7 million and \$2.5 million, respectively, which includes the cost of outside legal fees, insurance, and other expenses incurred in the management and defense of product liability matters. See note 6 to the notes to the financial statements "Contingent Liabilities" for further discussion of the Company's product liability.

Gross Margin—Gross margin was \$39.3 million or 25.1% of sales in 2007. This is an increase of \$11.3 million or 40.3% from 2006 gross margin of \$28.0 million or 16.7% of sales.

### Selling, General and Administrative

Selling, general and administrative expenses were \$28.8 million in 2007. This represents an increase of \$0.9 million or 3.0% from 2006 selling, general and administrative expenses of \$27.9 million. The increase reflects greater personnel-related expenses including equity-based compensation expense such as stock-option expense and performance-stock-option expense, partially offset by a reduction in advertising and sales promotion expenses.

### Pension Curtailment Charge

In 2007, the Company amended its hourly and salaried defined benefit pension plans so that employees will no longer accrue benefits under these plans effective December 31, 2007. This action “freezes” the benefits for all employees and prevents future hires from joining the plans, effective December 31, 2007. Starting in 2008, the Company will provide supplemental discretionary contributions to substantially all employees’ individual 401(k) accounts.

These amendments resulted in a \$1.2 million pension curtailment charge that was recognized in 2007.

### Other Operating Expenses (Income), net

Other operating expenses (income), net consist of the following:

| <u>Year ended December 31,</u>                      | <u>2007</u>   | <u>2006</u>    |
|---|---------------|----------------|
| Gain on sale of operating assets (a)                | \$ (472)      | \$(929)        |
| Impairment of operating assets (b)                  | 489           | 494            |
| Gain on sale of real estate (c)                     | (1,521)       | (397)          |
| <u>Impairment of real estate held for sale (d)</u>  | <u>1,775</u>  | <u>-</u>       |
| <u>Total other operating expenses (income), net</u> | <u>\$ 271</u> | <u>\$(832)</u> |

(a) The gain on sale of operating assets was generated primarily from the sale of used machinery and equipment. Most of the used machinery and equipment sold in 2007 and 2006 was related to titanium investment casting.

(b) In 2007, the Company recognized an impairment charge of \$0.5 million related to machinery and equipment previously in the Company’s Arizona investment casting operations. In 2006, the Company recognized an impairment charge of \$0.5 million related to building improvements at the Dorr Building. The Company had planned to establish a titanium investment castings foundry at Dorr, but that plan was aborted in 2006.

(c) On April 16, 2007, the Company sold a facility in Arizona for \$5.0 million. This facility had not been used in the Company’s operations for several years. The Company realized a gain of approximately \$1.5 million from this sale. In 2006, the \$0.4 million gain on sale of real estate reflects the sale of non-manufacturing real property. The Company has three additional non-manufacturing properties listed for sale, two in Connecticut and one in New Hampshire.

(d) In the fourth quarter of 2007, the Company recognized an asset impairment charge of \$1.8 million related to the Dorr Building, a non-manufacturing property in New Hampshire that has been for sale for an extended period of time without any meaningful market interest.

Operating Income—Operating Income was \$9.1 million or 5.8% of sales in 2007. This is an increase of \$8.2 million from 2006 operating income of \$0.9 million or 0.6% of sales.

#### Gain on Sale of Real Estate

In 2007, the \$5.2 million gain on sale of real estate reflects the sale of largely undeveloped non-manufacturing real property held for investment in March of 2007.

#### Interest income

Interest income was \$2.4 million in 2007. This represents an increase of \$1.3 million from 2006 interest income of \$1.1 million. The increase is attributable to increased principal invested in 2007 compared to 2006.

#### Income Taxes and Net Income

The effective income tax rate in 2007 was 38.0%. This compares favorably to the 2006 effective income tax rate of 40.1%. The reduction in 2007 results from an increase in the domestic production activities deduction.

As a result of the foregoing factors, consolidated net income was \$10.3 million in 2007. This represents an increase of \$9.2 million from 2006 consolidated net income of \$1.1 million.

### **Results of Operations**

*Year ended December 31, 2006, as compared to year ended December 31, 2005:*

#### Sales

Consolidated net sales were \$167.6 million in 2006. This represents an increase of \$12.9 million or 8.3% from 2005 consolidated net sales of \$154.7 million.

Firearms segment net sales were \$139.1 million in 2006. This represents an increase of \$6.3 million or 4.7% from 2005 firearm net sales of \$132.8 million. Firearms unit shipments increased 3% in 2006 due to increased shipments of revolvers, partially offset by a decline in shipments of shotguns, pistols, and rifles. Effective January 1, 2006, the Company instituted a unilateral minimum distributor resale price policy for its firearms, which remains in effect. This change in policy was well received by the Company's distributors and did not appear to have an adverse effect on the Company's firearm sales.

Casting segment net sales were \$28.5 million in 2006. This represents an increase of \$6.6 million or 30.1% from 2005 casting sales of \$21.9 million.

The casting sales increase was due primarily to the acceleration of titanium shipments related to the cessation of titanium casting operations, as previously announced by the Company in July 2006. Titanium casting sales accounted for \$16.2 million or 56% of casting sales in 2006. The Company continues to manufacture and sell steel investment castings for a wide variety of customers and end uses.

### Cost of Products Sold and Gross Margin

Consolidated cost of products sold was \$139.6 million in 2006. This represents an increase of \$14.8 million or 11.9% from 2005 consolidated cost of products sold of \$124.8 million.

The gross margin as a percent of sales was 16.7% in 2006. This represents a decline from the 2005 gross margin of 19.3% as illustrated below:

|  | December 31,     |              |                 |              |
|--|------------------|--------------|-----------------|--------------|
|  | 2006             |              | 2005            |              |
| Net sales  | \$167,620        | 100.0%       | \$154,722       | 100.0%       |
| Total cost of products sold,<br>before LIFO and overhead rate<br>inventory adjustments and<br>product liability (Note 1) | <u>135,881</u>   | <u>81.1%</u> | <u>121,198</u>  | <u>78.3%</u> |
| Performance gross margin*  | <u>31,739</u>    | <u>18.9%</u> | <u>33,524</u>   | <u>21.7%</u> |
| LIFO and overhead rate<br>inventory adjustments and<br>product liability (Note 2)  | <u>3,729</u>     | <u>2.2%</u>  | <u>3,628</u>    | <u>2.4%</u>  |
| Gross margin   | <u>\$ 28,010</u> | <u>16.7%</u> | <u>\$29,896</u> | <u>19.3%</u> |

\* Performance Gross Margin is a measure of gross margin before taking into account the impact of LIFO and overhead rate adjustments to inventory, and before product liability expenses.

Note 1: Performance gross margin was favorably impacted by stronger sales, and was adversely impacted by an excess and obsolete inventory charge of \$3.2 million, compared to \$0.5 million in 2005. The impact of the excess and obsolete inventory charge was 1.9% of sales in 2006 as compared to 0.3% of sales in 2005.

Note 2: Gross margin was favorably impacted by a LIFO liquidation of \$7.1 million and a reduction in product liability of \$2.4 million, and was adversely impacted by a reduction in inventory value of \$2.9 million related to overhead rate changes.

Excess and Obsolete Inventory—In prior years, the Company received one cancelable annual order in December from each of its distributors. Effective December 1, 2006 the Company changed the manner in which distributors order firearms, and began receiving firm, non-cancelable purchase orders on a frequent basis, with most orders for immediate delivery. In the past, the Company adjusted production schedules to consume on-hand raw material and WIP inventories, regardless of customer demand for the finished goods so produced. This practice led to increased investment in inventory, and an unbalanced finished goods inventory.

As a result of this new production philosophy, it became apparent the Company had inventory in excess of its needs over the foreseeable future. Given ever-changing market conditions, customer preferences and the anticipated introduction of new products, the Company concluded that it was not prudent nor

supportable to carry inventory at full cost beyond that needed during the next 36 months. Therefore the Company evaluated the adequacy of the excess and obsolescence inventory reserve and concluded that additional reserves were required to reflect the estimated recoverable value of excess inventories below LIFO carrying cost. The required reserve was estimated based on the following parameters, and resulted in an excess and obsolete expense of \$3.2 million and a reserve balance of \$5.5 million:

| <u>Projected Year<br/>Of Consumption</u> | <u>Required<br/>Reserve %</u> |
|--|-------------------------------|
| 2007                                     | 2%                            |
| 2008                                     | 10%                           |
| 2009                                     | 35%                           |
| 2010 and thereafter                      | 90%                           |

LIFO—During 2006, gross inventories were reduced by \$24.0 million. This reduction resulted in a liquidation of LIFO inventory quantities carried at lower costs that prevailed in prior years as compared with the current cost of purchases, the effect of which decreased costs of products sold by approximately \$7.1 million. There was no LIFO liquidation in 2005.

Reduction in inventory generated positive cash flow for the Company, partially offset by the tax impact of the consequent LIFO liquidation, which generated negative cash flow as it created taxable income, resulting in higher tax payments.

Product Liability—During the years ended December 31, 2006 and 2005, the Company incurred product liability expense of \$2.5 million and \$4.9 million, respectively, which includes the cost of outside legal fees, insurance, and other expenses incurred in the management and defense of product liability matters. See Footnote 6 “Contingent Liabilities” for further discussion of the Company’s product liability.

Overhead Rate Change—In 2006, the change in inventory value resulting from the change in the overhead rate used to absorb overhead expenses into inventory was a decrease of \$2.9 million. This reduction in inventory value resulted in an increase to cost of products sold.

In 2005, the change in inventory value as a result of a change in the overhead rate used to absorb overhead expenses into inventory was an increase of \$6.8 million. This increase in inventory value resulted in a decrease to cost of products sold.

Fourth Quarter Charge—In the fourth quarter of 2006, a \$2.5 million non-cash inventory valuation adjustment, net of the LIFO impact, was recorded to recognize inefficiencies in labor and overhead during a period of rapid inventory reduction. This over-absorption of labor and overhead was quantified by a physical inventory taken in the fourth quarter.

Due to the timing of the physical inventory, the Company was unable to quantify the impact of this delayed recognition of labor and overhead inefficiencies, if any, on the financial results of prior quarters. As a consequence, raw material and work in process physical inventories are being performed at the end of each quarter until a permanent corrective action is established and determined to be adequate, making these physical inventories unnecessary. These physical inventories were taken each quarter in 2007 and are expected to continue in 2008.

### Selling, General and Administrative

Selling, general and administrative expenses were \$27.9 million in 2006. This represents a decrease of \$0.2 million or 0.5% from 2005 selling, general and administrative expenses of \$28.1 million. The decrease reflects a reduction in advertising and sales promotion expenses, partially offset by increased personnel-related expenses including \$0.7 million related to the retirement of the former Chairman and Chief Executive Officer.

### Other Operating Expenses (Income), net

Other operating expenses (income), net consist of the following:

| <u>Year ended December 31,</u>                      | <u>2006</u>    | <u>2005</u>  |
|---|----------------|--------------|
| Gain on sale of operating assets (a)                | \$(929)        | -            |
| Impairment of operating assets (b)                  | 494            | 483          |
| Gain on sale of real estate (c)                     | (397)          | -            |
| <u>Total other operating expenses (income), net</u> | <u>\$(832)</u> | <u>\$483</u> |

(a) The gain on sale of operating assets is generated primarily from the sale of used machinery and equipment. Most of the machinery and equipment sold in 2006 was related to titanium investment casting.

(b) In 2006, the Company recognized an impairment charge of \$0.5 million related to building improvements at the Dorr Building. The Company had planned to establish a titanium investment castings foundry at Dorr, but that plan was aborted in 2006. In 2005, the Company recognized an impairment charge of \$0.5 million related to certain corporate assets and certain machinery and equipment in the castings segment.

(c) In 2006, the \$0.4 million gain on sale of real estate reflects the sale of non-manufacturing real property.

Operating Income—Operating Income was \$0.9 million or 0.6% of sales in 2006. This is a decrease of \$0.4 million from 2005 operating income of \$1.4 million or 0.9% of sales.

### Interest Income

Interest income was \$1.1 million in 2006. This represents an increase of \$0.3 million from 2005 interest income of \$0.8 million. The increase is attributable to more favorable interest rates in 2006..

### Income Taxes and Net Income

The effective income tax rate of 40.1% in 2006 remained consistent with the income tax rate in 2005.

As a result of the foregoing factors, consolidated net income was \$1.1 million in 2006. This represents an increase of \$0.2 million or 27.8% from 2005 consolidated net income of \$0.9 million.

## **Financial Condition**

### **Operations**

At December 31, 2007, the Company had cash, cash equivalents and short-term investments of \$35.6 million. The Company's pre-LIFO working capital of \$100.2 million, less the LIFO reserve of \$46.9 million, resulted in working capital of \$53.3 million and a current ratio of 3.6 to 1.

Cash provided by operating activities was \$17.5 million, \$30.2 million, and \$5.2 million in 2007, 2006, and 2005, respectively. The decrease in cash provided in 2007 compared to 2006 is principally attributable to comparable reductions in gross inventory, offset by a more significant reduction in the LIFO reserve in 2007, and increased voluntary pension plan contributions in 2007. The increase in cash provided in 2006 compared to 2005 is principally a result of a \$24.3 million decrease in inventory in 2006 and various fluctuations in operating asset and liability accounts during 2006 compared to 2005.

Third parties supply the Company with various raw materials for its firearms and castings, such as fabricated steel components, walnut, birch, beech, maple and laminated lumber for rifle and shotgun stocks, wax, ceramic material, metal alloys, various synthetic products and other component parts. There is a limited supply of these materials in the marketplace at any given time, which can cause the purchase prices to vary based upon numerous market factors. The Company believes that it has adequate quantities of raw materials in inventory to provide ample time to locate and obtain additional items at then-current market cost without interruption of its manufacturing operations. However, if market conditions result in a significant prolonged inflation of certain prices or if adequate quantities of raw materials can not be obtained, the Company's manufacturing processes could be interrupted and the Company's financial condition or results of operations could be materially adversely affected.

### **Investing and Financing**

Capital expenditures were \$4.5 million, \$3.9 million, and \$4.5 million in 2007, 2006, and 2005, respectively. In 2008, the Company expects to spend approximately \$5 million on capital expenditures to purchase tooling for new product introductions and to upgrade and modernize manufacturing equipment, primarily at the Newport Firearms and Pine Tree Castings Divisions. The Company finances, and intends to continue to finance, all of these activities with funds provided by operations and current cash and short-term investments.

On January 26, 2007, the Company announced that its Board of Directors authorized a stock repurchase program. During the fourth quarter of 2007, the Company repurchased 2,216,000 shares of its common stock, representing 9.7% of the outstanding shares, in the open market at an average price of \$8.99 per share. On September 26, 2006, the Company repurchased 4,272,000 shares of its common stock, representing 15.9% of the then outstanding shares, from entities controlled by members of the Ruger family at a price of \$5.90 per share. These purchases were made with cash held by the Company and no debt was incurred.

There were no dividends paid in 2007 or 2006. The payment of future dividends depends on many factors, including internal estimates of future performance, then-current cash and short-term investments, and the Company's need for funds. The Company does not expect to pay dividends in the near term.

On March 8, 2007, the Company sold 42 parcels of non-manufacturing real property for \$7.3 million to William B. Ruger, Jr., the Company's former Chief Executive Officer and Chairman of the Board. The



sale included substantially all of the Company's raw land real property assets in New Hampshire. The sales price was based upon an independent appraisal, and the Company recognized a gain of \$5.2 million on the sale.

On April 16, 2007, the Company sold a non-manufacturing facility in Arizona for \$5.0 million. This facility had not been used in the Company's operations for several years. The Company realized a gain of approximately \$1.5 million from this sale.

In 2007, the Company amended its hourly and salaried defined benefit pension plans so that employees will no longer accrue benefits under them effective December 31, 2007. This action "freezes" the benefits for all employees and prevents future hires from joining the plans, effective December 31, 2007. Starting in 2008, the Company will provide supplemental discretionary contributions to substantially all employees' individual 401(k) accounts.

In late 2007, after authorizing the "freeze" amendment to its hourly and salaried defined benefit pension plans, the Company contributed an additional \$5 million to the plans. The intent of this discretionary contribution is to reduce the amount of time that the Company will be required to continue to operate the frozen plans. The ongoing cost of running the plans (even if frozen) is approximately \$200,000 per year, which includes PBGC premiums, actuary and audit fees, and other expenses.

In 2008 and future years, the Company will be required to make cash contributions to the two defined benefit pension plans according to the new rules of the Pension Protection Act of 2006. The annual contributions will be based on the amount of the unfunded plan liabilities derived from the frozen benefits and will not include liabilities for any future accrued benefits for any new or existing participants. The total amount of these future cash contributions will be dependent on the investment returns generated by the plans' assets and the then-applicable discount rates used to calculate the plans' liabilities. The 2008 cash contribution for the defined benefit plans is not expected to exceed \$1 million.

In future years, the total annual cash outlays for retirement benefits, which would include the continuing funding of the two defined benefit pension plans and the new supplemental discretionary 401(k) contributions, are expected to be comparable to the previous retirement funding levels.

In February 2008, the Company made lump sum benefit payments to two participants in its only non-qualified defined benefit plan, the Supplemental Executive Retirement Plan (SERP). These payments, which totaled \$2.1 million, represented the actuarial present value of the participants' accrued benefit as of the date of payment. Only one, retired participant remains in this plan.

Historically, the Company has not required external financing. Based on its unencumbered assets, the Company believes it has the ability to raise substantial amounts of cash through issuance of short-term or long-term debt. In the fourth quarter of 2007, the Company secured a \$25 million credit facility, which terminates on December 13, 2008. This credit facility remains unused.

#### Contractual Obligations

The table below summarizes the Company's significant contractual obligations at December 31, 2007, and the effect such obligations are expected to have on the Company's liquidity and cash flows in future periods. This table excludes amounts already recorded on the Company's balance sheet as current liabilities at December 31, 2007.

“Purchase Obligations” as used in the below table includes all agreements to purchase goods or services that are enforceable and legally binding on the Company and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Certain of the Company’s purchase orders or contracts for the purchase of raw materials and other goods and services that may not necessarily be enforceable or legally binding on the Company, are also included in “Purchase Obligations” in the table. Certain of the Company’s purchase orders or contracts therefore included in the table may represent authorizations to purchase rather than legally binding agreements. The Company expects to fund all of these commitments with cash flows from operations and current cash and short-term investments.

| <b>Contractual Obligations</b>                         | <b>Payment due by period (in thousands)</b> |                             |                      |                      |                              |
|--|---|-----------------------------|----------------------|----------------------|------------------------------|
|  | <b>Total</b>                                | <b>Less than<br/>1 year</b> | <b>1-3<br/>years</b> | <b>3-5<br/>years</b> | <b>More than<br/>5 years</b> |
| Long-Term Debt Obligations                             | -   | -                           | -                    | -                    | -                            |
| Capital Lease Obligations                              | -   | -                           | -                    | -                    | -                            |
| Operating Lease Obligations                            | -   | -                           | -                    | -                    | -                            |
| Purchase Obligations                                   | \$25,300                                    | \$25,300                    | -                    | -                    | -                            |
| Other Long-Term Liabilities                            |   |                             |                      |                      |                              |
| Reflected on the Registrant’s Balance Sheet under GAAP | -   | -                           | -                    | -                    | -                            |
| <b>Total</b>   | <b>\$25,300</b>                             | <b>\$25,300</b>             | <b>-</b>             | <b>-</b>             | <b>-</b>                     |

The expected timing of payment of the obligations discussed above is estimated based on current information. Timing of payments and actual amounts paid may be different depending on the time of receipt of goods or services or changes to agreed-upon amounts for some obligations.

The Company adopted the provisions of FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes,” on January 1, 2007. Upon the adoption of FIN 48, the Company commenced a review of all open tax years in all jurisdictions. The Company does not believe it has included any “uncertain tax positions” in its Federal income tax return or any of the state income tax returns it is currently filing. The Company has made an evaluation of the potential impact of additional state taxes being assessed by jurisdictions in which the Company does not currently consider itself liable. The Company does not anticipate that such additional taxes, if any, would result in a material change to its financial position. However, the Company anticipates that it is more likely than not that additional state tax liabilities in the range of \$0.4 to \$0.7 million exist. The Company had previously recorded \$0.4 million relating to these additional state income taxes, including approximately \$0.2 million for the payment of interest and penalties. This amount is included in income taxes payable at December 31, 2007. In connection with the adoption of FIN 48, the Company will include interest and penalties related to uncertain tax positions as a component of its provision for taxes.

## **Firearms Legislation**

*(The following disclosures within “Firearms Legislation” are identical to the disclosures within Item 1A-Risk Factors “Firearms Legislation.”)*

The sale, purchase, ownership, and use of firearms are subject to thousands of federal, state and local governmental regulations. The basic federal laws are the National Firearms Act, the Federal Firearms Act, and the Gun Control Act of 1968. These laws generally prohibit the private ownership of fully automatic weapons and place certain restrictions on the interstate sale of firearms unless certain licenses are obtained. The Company does not manufacture fully automatic weapons, other than for the law enforcement market, and holds all necessary licenses under these federal laws. From time to time, congressional committees review proposed bills relating to the regulation of firearms. These proposed bills generally seek either to restrict or ban the sale and, in some cases, the ownership of various types of firearms. Several states currently have laws in effect similar to the aforementioned legislation.

Until November 30, 1998, the “Brady Law” mandated a nationwide five-day waiting period and background check prior to the purchase of a handgun. As of November 30, 1998, the National Instant Check System, which applies to both handguns and long guns, replaced the five-day waiting period. The Company believes that the “Brady Law” and the National Instant Check System have not had a significant effect on the Company’s sales of firearms, nor does it anticipate any impact on sales in the future. On September 13, 1994, the “Crime Bill” banned so-called “assault weapons.” All the Company’s then-manufactured commercially-sold long guns were exempted by name as “legitimate sporting firearms.” This ban expired by operation of law on September 13, 2004. The Company remains strongly opposed to laws which would restrict the rights of law-abiding citizens to lawfully acquire firearms. The Company believes that the lawful private ownership of firearms is guaranteed by the Second Amendment to the United States Constitution and that the widespread private ownership of firearms in the United States will continue. However, there can be no assurance that the regulation of firearms will not become more restrictive in the future and that any such restriction would not have a material adverse effect on the business of the Company.

## **Firearms Litigation**

*(The following disclosures within “Firearms Litigation” are identical to the disclosures within Item 1A-Risk Factors “Firearms Litigation” and Note 6 to the notes to the financial statements-Contingent Liabilities.)*

As of December 31, 2007, the Company is a defendant in approximately 5 lawsuits involving its products and is aware of certain other such claims. These lawsuits and claims fall into two categories:

- (i) those that claim damages from the Company related to allegedly defective product design which stem from a specific incident. Pending lawsuits and claims are based principally on the theory of “strict liability” but also may be based on negligence, breach of warranty, and other legal theories; and
- (ii) those brought by cities or other governmental entities, and individuals against firearms manufacturers, distributors and dealers seeking to recover damages allegedly arising out of the misuse of firearms by third parties in the commission of homicides, suicides and other shootings involving juveniles and adults. The complaints by municipalities seek damages, among other things, for the costs of medical care, police and emergency services, public

health services, and the maintenance of courts, prisons, and other services. In certain instances, the plaintiffs seek to recover for decreases in property values and loss of business within the city due to criminal violence. In addition, nuisance abatement and/or injunctive relief is sought to change the design, manufacture, marketing and distribution practices of the various defendants. These suits allege, among other claims, strict liability or negligence in the design of products, public nuisance, negligent entrustment, negligent distribution, deceptive or fraudulent advertising, violation of consumer protection statutes and conspiracy or concert of action theories. Most of these cases do not allege a specific injury to a specific individual as a result of the misuse or use of any of the Company's products.

The Company has expended significant amounts of financial resources and management time in connection with product liability litigation. Management believes that, in every case involving firearms, the allegations are unfounded, and that the shootings and any results therefrom were due to negligence or misuse of the firearms by third-parties or the claimant, and that there should be no recovery against the Company. Defenses further exist to the suits brought by governmental entities based, among other reasons, on established state law precluding recovery for essential government services, the remoteness of the claims, the types of damages sought to be recovered, and limitations on the extraterritorial authority which may be exerted by a city, municipality, county or state under state and federal law, including State and Federal Constitutions.

The only case against the Company alleging liability for criminal shootings by third-parties to ever be permitted to go before a constitutional jury, Hamilton, et al. v. Accu-tek, et al., resulted in a defense verdict in favor of the Company on February 11, 1999. In that case, numerous firearms manufacturers and distributors had been sued, alleging damages as a result of alleged negligent sales practices and "industry-wide" liability. The Company and its marketing and distribution practices were exonerated from any claims of negligence in each of the seven cases decided by the jury. In subsequent proceedings involving other defendants, the New York Court of Appeals as a matter of law confirmed that 1) no legal duty existed under the circumstances to prevent or investigate criminal misuses of a manufacturer's lawfully made products; and 2) liability of firearms manufacturers could not be apportioned under a market share theory. More recently, the New York Court of Appeals on October 21, 2003 declined to hear the appeal from the decision of the New York Supreme Court, Appellate Division, affirming the dismissal of New York Attorney General Eliot Spitzer's public nuisance suit against the Company and other manufacturers and distributors of firearms. In its decision, the Appellate Division relied heavily on Hamilton in concluding that it was "legally inappropriate," "impractical," "unrealistic" and "unfair" to attempt to hold firearms manufacturers responsible under theories of public nuisance for the criminal acts of others.

Of the lawsuits brought by municipalities, counties or a state Attorney General, twenty have been concluded: Atlanta – dismissal by intermediate Appellate Court, no further appeal; Bridgeport – dismissal affirmed by Connecticut Supreme Court; County of Camden – dismissal affirmed by U.S. Third Circuit Court of Appeals; Miami – dismissal affirmed by intermediate appellate court, Florida Supreme Court declined review; New Orleans – dismissed by Louisiana Supreme Court, United States Supreme Court declined review; Philadelphia – U.S. Third Circuit Court of Appeals affirmed dismissal, no further appeal; Wilmington – dismissed by trial court, no appeal; Boston – voluntary dismissal with prejudice by the City at the close of fact discovery; Cincinnati – voluntarily withdrawn after a unanimous vote of the city council; Detroit – dismissed by Michigan Court of Appeals, no appeal; Wayne County – dismissed by Michigan Court of Appeals, no appeal; New York State – Court of Appeals denied plaintiff's petition for leave to appeal the Intermediate Appellate Court's dismissal, no

further appeal; Newark – Superior Court of New Jersey Law Division for Essex County dismissed the case with prejudice; City of Camden – dismissed on July 7, 2003, not reopened; Jersey City – voluntarily dismissed and not re-filed; St. Louis – Missouri Supreme Court denied plaintiffs’ motion to appeal Missouri Appellate Court’s affirmation of dismissal; Chicago – Illinois Supreme Court affirmed trial court’s dismissal; and Los Angeles City, Los Angeles County, San Francisco – Appellate Court affirmed summary judgment in favor of defendants, no further appeal; and Cleveland – dismissed on January 24, 2006 for lack of prosecution.

The dismissal of the Washington, D.C. municipal lawsuit was sustained on appeal, but individual plaintiffs were permitted to proceed to discovery and attempt to identify the manufacturers of the firearms used in their shootings as “machine guns” under the city’s “strict liability” law. On April 21, 2005, the D.C. Court of Appeals, in an *en banc* hearing, unanimously dismissed all negligence and public nuisance claims, but let stand individual claims based upon a Washington, D.C. act imposing “strict liability” for manufacturers of “machine guns.” Based on present information, none of the Company’s products has been identified with any of the criminal assaults which form the basis of the individual claims. The writ of certiorari to the United States Supreme Court regarding the constitutionality of the Washington, D.C. act was denied and the case was remanded to the trial court for further proceedings. The defendants subsequently moved to dismiss the case based upon the Protection of Lawful Commerce in Arms Act, which motion was granted on May 22, 2006. The individual plaintiffs and the District of Columbia, which has subrogation claims in regard to the individual plaintiffs, appealed. On January 10, 2008, the District of Columbia Court of Appeals unanimously upheld the dismissal. Plaintiffs have until February 25, 2008, to move for rehearing *en banc*.

The Indiana Court of Appeals affirmed the dismissal of the Gary case by the trial court, but the Indiana Supreme Court reversed this dismissal and remanded the case for discovery proceedings on December 23, 2003. Gary is scheduled to begin trial in 2009. The defendants filed a motion to dismiss pursuant to the Protection of Lawful Commerce in Arms Act (“PLCAA”). The state court judge held the PLCAA unconstitutional and the defendants filed a motion with the Indiana Court of Appeals asking it to accept interlocutory appeal on the issue, which appeal was accepted on February 5, 2007. On October 29, 2007, the Indiana Appellate Court affirmed, holding that the PLCAA does not apply to the City’s claims. A petition for rehearing was filed in the Appellate Court and denied on January 9, 2008. A Petition to Transfer the appeal to the Supreme Court of Indiana was filed on February 7, 2008.

In the previously reported New York City municipal case, the defendants moved to dismiss the suit pursuant to the Protection of Lawful Commerce in Arms Act. The trial judge found the Act to be constitutional but denied the defendants’ motion to dismiss the case, stating that the Act was not applicable to the suit. The defendants were given leave to appeal and in fact have appealed the decision to the U.S. Court of Appeals for the Second Circuit. That appeal remains pending.

In the NAACP case, on May 14, 2003, an advisory jury returned a verdict rejecting the NAACP’s claims. On July 21, 2003, Judge Jack B. Weinstein entered an order dismissing the NAACP lawsuit, but this order contained lengthy dicta which defendants believe are contrary to law and fact. Appeals by both sides were filed, but plaintiffs withdrew their appeal. On August 3, 2004, the United States Court of Appeals for the Second Circuit granted the NAACP’s motion to dismiss the defendants’ appeal of Judge Weinstein’s order denying defendants’ motion to strike his dicta made in his order dismissing the NAACP’s case, and the defendants’ motion for summary disposition was denied as moot. The ruling of the Second Circuit effectively confirmed the decision in favor of defendants and brought this matter to a conclusion.

Legislation has been passed in approximately 34 states precluding suits of the type brought by the municipalities mentioned above. On the Federal level, the “Protection of Lawful Commerce in Arms Act” was signed by President Bush on October 26, 2005. The Act requires dismissal of suits against manufacturers arising out of the lawful sale of their products for harm resulting from the criminal or unlawful misuse of a firearm by a third party. The Company is pursuing dismissal of each action involving such claims, including the municipal cases described above. The Company was voluntarily dismissed with prejudice on March 23, 2007 from the previously reported Arnold case. The matter was thus concluded with no payment by the Company.

Punitive damages, as well as compensatory damages, are demanded in certain of the lawsuits and claims. Aggregate claimed amounts presently exceed product liability accruals and applicable insurance coverage. For claims made after July 10, 2000, coverage is provided on an annual basis for losses exceeding \$5 million per claim, or an aggregate maximum loss of \$10 million annually, except for certain new claims which might be brought by governments or municipalities after July 10, 2000, which are excluded from coverage.

Product liability claim payments are made when appropriate if, as, and when claimants and the Company reach agreement upon an amount to finally resolve all claims. Legal costs are paid as the lawsuits and claims develop, the timing of which may vary greatly from case to case. A time schedule cannot be determined in advance with any reliability concerning when payments will be made in any given case.

Provision is made for product liability claims based upon many factors related to the severity of the alleged injury and potential liability exposure, based upon prior claim experience. Because our experience in defending these lawsuits and claims is that unfavorable outcomes are typically not probable or estimable, only in rare cases is an accrual established for such costs. In most cases, an accrual is established only for estimated legal defense costs. Product liability accruals are periodically reviewed to reflect then-current estimates of possible liabilities and expenses incurred to date and reasonably anticipated in the future. Threatened product liability claims are reflected in our product liability accrual on the same basis as actual claims; i.e., an accrual is made for reasonably anticipated possible liability and claims-handling expenses on an ongoing basis.

A range of reasonably possible loss relating to unfavorable outcomes cannot be made. However, in product liability cases in which a dollar amount of damages is claimed, the amount of damages claimed, which totaled \$5 million and \$0 at December 31, 2007 and 2006, respectively, are set forth as an indication of possible maximum liability that the Company might be required to incur in these cases (regardless of the likelihood or reasonable probability of any or all of this amount being awarded to claimants) as a result of adverse judgments that are sustained on appeal.

As of December 31, 2007 and 2006, the Company was a defendant in 5 and 4 lawsuits, respectively, involving its products and is aware of other such claims. During the year ended December 31, 2007 and 2006, respectively, 2 and 2 claims were filed against the Company, 1 and 2 claims were dismissed, and 0 and 2 claims were settled. The average cost per settled claim was \$47,000 in 2006.

During the years ended December 31, 2007 and 2006, the Company incurred product liability expense of \$1.7 million and \$2.5 million, respectively, which includes the cost of outside legal fees, insurance, and other expenses incurred in the management and defense of product liability matters.

The Company management monitors the status of known claims and the product liability accrual, which includes amounts for asserted and unasserted claims. While it is not possible to forecast the outcome of litigation or the timing of costs, in the opinion of management, after consultation with special and corporate counsel, it is not probable and is unlikely that litigation, including punitive damage claims, will have a material adverse effect on the financial position of the Company, but may have a material impact on the Company's financial results for a particular period.

The Company has reported all cases instituted against it through September 30, 2007 and the results of those cases, where terminated, to the S.E.C. on its previous Form 10-K and 10-Q reports, to which reference is hereby made.

### **Balance Sheet Rollforward for Product Liability Reserve**

*(Dollars in thousands)*

| Cash Payments |  |                                    |                   |                    |                       |                   |                               |
|---------------|--|------------------------------------|-------------------|--------------------|-----------------------|-------------------|-------------------------------|
|               | Balance<br>Beginning<br>of Year<br>(a) | Accrued<br>Legal<br>Expense<br>(b) | Legal<br>Fees (c) | Settlements<br>(d) | Insurance<br>Premiums | Admin.<br>Expense | Balance<br>End of<br>Year (a) |
| 2005          | \$3,132                                | \$2,514                            | \$(2,935)         | (515)              | N/A                   | N/A               | \$2,196                       |
| 2006          | 2,196                                  | 688                                | (1,000)           | (143)              | N/A                   | N/A               | 1,741                         |
| 2007          | 1,741                                  | 639                                | (447)             | -                  | N/A                   | N/A               | 1,933                         |

### **Income Statement Detail for Product Liability Expense**

*(Dollars in thousands)*

|      | Accrued<br>Legal<br>Expense<br>(b) | Insurance<br>Premium<br>Expense<br>(e) | Admin.<br>Expense<br>(f) | Total<br>Product<br>Liability<br>Expense |
|------|------------------------------------|--|--------------------------|--|
| 2005 | \$2,514                            | \$1,338                                | \$1,041                  | \$4,893                                  |
| 2006 | 688                                | 1,141                                  | 691                      | 2,520                                    |
| 2007 | 639                                | 748                                    | 299                      | 1,686                                    |

### **Notes**

- (a) The beginning and ending liability balances represent accrued legal fees only. Settlements and administrative costs are expensed as incurred. Only in rare instances is an accrual established for settlements.
- (b) The expense accrued in the liability is for legal fees only.
- (c) Legal fees represent payments to outside counsel related to product liability matters.

- (d) Settlements represent payments made to plaintiffs or allegedly injured parties in exchange for a full and complete release of liability.
- (e) Insurance expense represents the cost of insurance premiums.
- (f) Administrative expense represents personnel related and travel expenses of Company employees and firearm experts related to the management and monitoring of product liability matters.

There were no insurance recoveries during any of the above years.

### **Other Operational Matters**

In the normal course of its manufacturing operations, the Company is subject to occasional governmental proceedings and orders pertaining to waste disposal, air emissions and water discharges into the environment. The Company believes that it is generally in compliance with applicable environmental regulations and the outcome of such proceedings and orders will not have a material adverse effect on the financial position or results of operations of the Company.

The Company self-insures a significant amount of its product liability, workers compensation, medical, and other insurance. It also carries significant deductible amounts on various insurance policies.

The valuation of the future defined benefit pension obligations at December 31, 2007 and 2006 indicated that these plans were underfunded by \$4.8 million and \$7.6 million, respectively, and resulted in a cumulative other comprehensive loss of \$13.4 million and \$12.4 million on the Company's balance sheet at December 31, 2007 and 2006, respectively.

The Company expects to realize its deferred tax assets through tax deductions against future taxable income.

### **Critical Accounting Policies**

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make assumptions and estimates that affect the reported amounts of assets and liabilities as of the balance sheet date and revenues and expenses recognized and incurred during the reporting period then ended. The Company bases estimates on prior experience, facts and circumstances, and other assumptions, including those reviewed with actuarial consultants and independent counsel, when applicable, that are believed to be reasonable. However, actual results may differ from these estimates.

The Company believes the determination of its product liability accrual is a critical accounting policy. The Company's management reviews every lawsuit and claim at the outset and is in contact with independent and corporate counsel on an ongoing basis. The provision for product liability claims is based upon many factors, which vary for each case. These factors include the type of claim, nature and extent of injuries, historical settlement ranges, jurisdiction where filed, and advice of counsel. An accrual is established for each lawsuit and claim, when appropriate, based on the nature of each such lawsuit or claim.



Amounts are charged to product liability expense in the period in which the Company becomes aware that a claim or, in some instances a threat of claim, has been made when potential losses or costs of defense can be reasonably estimated. Such amounts are determined based on the Company's experience in defending similar claims. Occasionally, charges are made for claims made in prior periods because the cumulative actual costs incurred for that claim, or reasonably expected to be incurred in the future, exceed amounts already provided. Likewise credits may be taken if cumulative actual costs incurred for that claim, or reasonably expected to be incurred in the future, are less than amounts previously provided.

While it is not possible to forecast the outcome of litigation or the timing of costs, in the opinion of management, after consultation with independent and corporate counsel, it is not probable and is unlikely that litigation, including punitive damage claims, will have a material adverse effect on the financial position of the Company, but may have a material impact on the Company's financial results for a particular period.

The Company believes the valuation of its inventory and the related excess and obsolescence reserve is also a critical accounting policy. Inventories are carried at the lower of cost, principally determined by the last-in, first-out (LIFO) method, or market. An actual valuation of inventory under the LIFO method is made at the end of each year based on the inventory levels and prevailing inventory costs existing at that time.

The Company determines its excess and obsolescence reserve by projecting the year in which inventory will be consumed into a finished product. Given ever-changing market conditions, customer preferences and the anticipated introduction of new products, it does not seem prudent nor supportable to carry inventory at full cost beyond that needed during the next 36 months. Therefore, the Company estimates its excess and obsolescence inventory reserve based on the following parameters:

| <u>Projected Year<br/>Of Consumption</u> | <u>Required<br/>Reserve %</u> |
|--|-------------------------------|
| 2008                                     | 2%                            |
| 2009                                     | 10%                           |
| 2010                                     | 35%                           |
| 2011 and thereafter                      | 90%                           |

### **Recent Accounting Pronouncements**

In September 2006, FASB issued FAS No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions of FAS 157 are effective for the fiscal year beginning January 1, 2008. The FASB has deferred the implementation of FAS 157 by one year for certain non-financial assets and liabilities such as this will be effective for the fiscal year beginning January 1, 2009. The adoption of FAS 157 is not expected to have a material impact on the Company's financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("FAS 141R"). FAS 141R establishes principles and requirements for how an acquirer recognizes and

measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquiree and the goodwill acquired. FAS 141R also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. FAS 141R is effective for the fiscal year beginning January 1, 2009, and will be adopted by the Company in the first quarter of 2009. The adoption of FAS 141R is not expected to have a material impact on the Company's financial position, results of operations and cash flows.

### **Forward-Looking Statements and Projections**

The Company may, from time to time, make forward-looking statements and projections concerning future expectations. Such statements are based on current expectations and are subject to certain qualifying risks and uncertainties, such as market demand, sales levels of firearms, anticipated castings sales and earnings, the need for external financing for operations or capital expenditures, the results of pending litigation against the Company including lawsuits filed by mayors, state attorneys general and other governmental entities and membership organizations, and the impact of future firearms control and environmental legislation, any one or more of which could cause actual results to differ materially from those projected. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date made. The Company undertakes no obligation to publish revised forward-looking statements to reflect events or circumstances after the date such forward-looking statements are made or to reflect the occurrence of subsequent unanticipated events.

### **ITEM 7A—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company is exposed to changing interest rates on its investments, which consists primarily of United States Treasury instruments with short-term (less than one year) maturities and cash. The interest rate market risk implicit in the Company's investments at any given time is low, as the investments mature within short periods and the Company does not have significant exposure to changing interest rates on invested cash.

The Company has not undertaken any actions to cover interest rate market risk and is not a party to any interest rate market risk management activities.

A hypothetical ten percent change in market interest rates over the next year would not materially impact the Company's earnings or cash flows. A hypothetical ten percent change in market interest rates would not have a material effect on the fair value of the Company's investments.

## ITEM 8—FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

### INDEX TO FINANCIAL STATEMENTS

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## Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders  
Sturm, Ruger & Company, Inc.

We have audited Sturm, Ruger & Company, Inc.'s internal control over financial reporting as of December 31, 2007, based on *criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. Sturm, Ruger & Company, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Sturm, Ruger & Company, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on *criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of Sturm, Ruger & Company, Inc. as of December 31, 2007 and 2006, and the related statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2007 and our report dated February 22, 2008 expressed an unqualified opinion.

/s/McGladrey & Pullen, LLP  
Stamford, Connecticut  
February 22, 2008

## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders  
Sturm, Ruger & Company, Inc.

We have audited the balance sheets of Sturm, Ruger & Company, Inc. as of December 31, 2007 and 2006, and the related statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2007. Our audits also included the financial statement schedule of Sturm, Ruger & Company, Inc. listed in Item 15(a). These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Sturm, Ruger & Company, Inc. as of December 31, 2007 and 2006, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Sturm, Ruger & Company, Inc.'s internal control over financial reporting as of December 31, 2007, based on *criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)* and our report dated February 22, 2008 expressed an unqualified opinion on the effectiveness of Sturm, Ruger & Company, Inc.'s internal control over financial reporting.

/s/McGladrey & Pullen, LLP  
Stamford, Connecticut  
February 22, 2008

Balance Sheets

*(Dollars in thousands, except per share data)*

| <i>December 31,</i>                       | <b>2007</b> | 2006      |
|---|-------------|-----------|
| <b>Assets</b>                             |             |           |
| Current Assets                            |             |           |
| Cash and cash equivalents                 | \$ 5,106    | \$ 7,316  |
| Short-term investments                    | 30,504      | 22,026    |
| Trade receivables, net                    | 15,636      | 18,007    |
| Gross inventories:                        | 64,330      | 87,477    |
| Less LIFO reserve                         | (46,890)    | (57,555)  |
| Less excess and obsolescence reserve      | (4,143)     | (5,516)   |
| Net inventories                           | 13,297      | 24,406    |
| Deferred income taxes                     | 5,878       | 8,347     |
| Prepaid expenses and other current assets | 3,091       | 1,683     |
| Total Current Assets                      | 73,512      | 81,785    |
| Property, Plant, and Equipment            | 126,496     | 128,042   |
| Less allowances for depreciation          | (104,418)   | (105,081) |
| Net property, plant and equipment         | 22,078      | 22,961    |
| Deferred income taxes                     | 3,626       | 3,630     |
| Other assets                              | 2,666       | 8,690     |
| Total Assets                              | \$101,882   | \$117,066 |

*See accompanying notes to financial statements.*

December 31,

2007

2006

**Liabilities and Stockholders' Equity**

Current Liabilities

|   |          |          |
|---|----------|----------|
| Trade accounts payable and accrued expenses | \$ 8,102 | \$ 6,342 |
| Product liability                           | 1,208    | 904      |
| Employee compensation and benefits          | 4,860    | 6,416    |
| Workers' compensation                       | 5,667    | 6,547    |
| Income taxes payable                        | 411      | 1,054    |
| Total Current Liabilities                   | 20,248   | 21,263   |

|                           |       |       |
|---------------------------|-------|-------|
| Accrued pension liability | 4,840 | 7,640 |
| Product liability         | 725   | 837   |

Contingent liabilities (Note 6) - -

Stockholders' Equity

Common stock, non-voting, par value \$1:

Authorized shares – 50,000; none issued

Common stock, par value \$1:

Authorized shares – 40,000,000

2007-22,787,812 issued,

20,571,817 outstanding

2006-22,638,700 issued and outstanding

|  |          |          |
|--|----------|----------|
| Additional paid-in capital                       | 1,836    | 2,615    |
| Retained earnings                                | 84,834   | 74,505   |
| Less: Treasury stock – 2,215,995 shares, at cost | (20,000) | -        |
| Accumulated other comprehensive loss             | (13,389) | (12,433) |

Total Stockholders' Equity 76,069 87,326

Total Liabilities and Stockholders' Equity \$ 101,882 \$117,066

*See accompanying notes to financial statements.*

Statements of Income*(In thousands, except per share data)*

| Year ended December 31,                | 2007      | 2006      | 2005      |
|--|-----------|-----------|-----------|
| Net firearms sales                     | \$144,222 | \$139,110 | \$132,805 |
| Net castings sales                     | 12,263    | 28,510    | 21,917    |
| Total net sales                        | 156,485   | 167,620   | 154,722   |
| Cost of products sold                  | 117,186   | 139,610   | 124,826   |
| Gross profit                           | 39,299    | 28,010    | 29,896    |
| Expenses:                              |           |           |           |
| Selling                                | 15,092    | 15,810    | 17,271    |
| General and administrative             | 13,678    | 12,110    | 10,788    |
| Pension plan curtailment charge        | 1,143     | -         | -         |
| Other operating expenses (income), net | 271       | (832)     | 483       |
| Total expenses                         | 30,184    | 27,088    | 28,542    |
| Operating income                       | 9,115     | 922       | 1,354     |
| Other income:                          |           |           |           |
| Gain on sale of real estate            | 5,168     | -         | -         |
| Interest income                        | 2,368     | 1,062     | 786       |
| Other income (expense), net            | 8         | (141)     | (698)     |
| Total other income, net                | 7,544     | 921       | 88        |
| Income before income taxes             | 16,659    | 1,843     | 1,442     |
| Income taxes                           | 6,330     | 739       | 578       |
| Net income                             | \$ 10,329 | \$ 1,104  | \$ 864    |
| Basic and Diluted Earnings Per Share   | \$ 0.46   | \$ 0.04   | \$ 0.03   |
| Cash Dividends Per Share               | \$ 0.00   | \$ 0.00   | \$ 0.30   |

*See accompanying notes to financial statements.*



Statements of Stockholders' Equity  
(Dollars in thousands)

|  | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Total           |
|--|-----------------|----------------------------------|----------------------|-------------------|---|-----------------|
| Balance at December 31, 2004   | \$26,911        | \$2,508                          | \$101,543            | -                 | \$(10,275)                                    | \$120,687       |
| Net income   |                 |                                  | 864                  |                   |   | 864             |
| Additional minimum pension liability, net of deferred taxes of \$1,267 |                 |                                  |                      |                   | (1,900)                                       | <u>(1,900)</u>  |
| Comprehensive income   |                 |                                  |                      |                   |   | <u>(1,036)</u>  |
| Cash dividends   |                 |                                  | (8,073)              |                   |   | <u>(8,073)</u>  |
| Balance at December 31, 2005   | 26,911          | 2,508                            | 94,334               | -                 | (12,175)                                      | 111,578         |
| Net income   |                 |                                  | 1,104                |                   |   | 1,104           |
| Pension liability, net of deferred taxes of \$172                      |                 |                                  |                      |                   | (258)   | <u>(258)</u>    |
| Stock-based compensation, net of tax                                   |                 | 107                              |                      |                   |   | <u>107</u>      |
| Comprehensive income   |                 |                                  |                      |                   |   | <u>953</u>      |
| Repurchase of 4,272,000 Shares of common stock                         | (4,272)         |                                  | (20,933)             |                   |   | <u>(25,205)</u> |
| Balance at December 31, 2006   | 22,639          | 2,615                            | 74,505               | -                 | (12,433)                                      | 87,326          |
| Net income   |                 |                                  | 10,329               |                   |   | 10,329          |
| Pension liability, net of deferred taxes of \$637                      |                 |                                  |                      |                   | (956)   | <u>(956)</u>    |
| Stock-based compensation, net of tax                                   | 30              | 1,017                            |                      |                   |   | <u>1,047</u>    |
| Comprehensive income   |                 |                                  |                      |                   |   | <u>10,420</u>   |
| Exercise of options  | 119             | (1,796)                          |                      |                   |   | <u>(1,677)</u>  |
| Repurchase of 2,216,000 shares of common stock                         |                 |                                  |                      | (20,000)          |   | <u>(20,000)</u> |
| Balance at December 31, 2007   | \$22,788        | \$1,836                          | \$84,834             | \$(20,000)        | \$(13,389)                                    | \$76,069        |

See accompanying notes to financial statements.

Statements of Cash Flows  
(In thousands)

| Year ended December 31,   | 2007      | 2006      | 2005      |
|---|-----------|-----------|-----------|
| <b>Operating Activities</b>   |           |           |           |
| Net income  | \$ 10,329 | \$ 1,104  | \$ 864    |
| Adjustments to reconcile net income to cash provided by operating activities: |           |           |           |
| Depreciation  | 4,372     | 3,852     | 5,440     |
| Impairment of assets  | 2,264     | 494       | 483       |
| Pension plan curtailment charge   | 1,143     | -         | -         |
| Gain on sale of assets  | (7,161)   | (1,326)   | -         |
| Deferred income taxes   | 2,473     | (2,759)   | (328)     |
| Changes in operating assets and liabilities:                                  |           |           |           |
| Trade receivables   | 2,371     | (2,230)   | 305       |
| Inventories   | 11,109    | 24,320    | 1,659     |
| Trade accounts payable and other liabilities                                  | (1,001)   | 3,023     | 13        |
| Product liability   | 192       | (455)     | (936)     |
| Prepaid expenses and other assets   | (6,128)   | 4,077     | (2,422)   |
| Income taxes  | (643)     | 119       | 167       |
| Cash provided by operating activities   | 19,320    | 30,219    | 5,245     |
| <b>Investing Activities</b>   |           |           |           |
| Property, plant, and equipment additions                                      | (4,468)   | (3,906)   | (4,460)   |
| Purchases of short-term investments   | (51,328)  | (114,585) | (125,245) |
| Proceeds from sales or maturities of short-term investments                   | 42,850    | 114,485   | 131,749   |
| Net proceeds from sale of assets  | 12,542    | 2,251     | -         |
| Cash (used for) provided by investing activities                              | (404)     | (1,755)   | 2,044     |
| <b>Financing Activities</b>   |           |           |           |
| Cashless exercise of stock options  | (1,126)   | -         | -         |
| Repurchase of common stock  | (20,000)  | (25,205)  | -         |
| Dividends paid  | -         | -         | (8,073)   |
| Cash used for financing activities  | (21,126)  | (25,205)  | (8,073)   |
| Increase (Decrease) in cash and cash equivalents                              | (2,210)   | 3,259     | (784)     |
| Cash and cash equivalents at beginning of year                                | 7,316     | 4,057     | 4,841     |
| Cash and Cash Equivalents at End of Year                                      | \$ 5,106  | \$ 7,316  | \$ 4,057  |

See accompanying notes to financial statements.

## Notes to Financial Statements

### 1. Significant Accounting Policies

#### Organization

Sturm, Ruger & Company, Inc. (the “Company”) is principally engaged in the design, manufacture, and sale of firearms to domestic customers. Approximately 92% of the Company’s total sales for the year ended December 31, 2007 were from the firearms segment. Export sales represent less than 6% of firearms sales. The Company’s design and manufacturing operations are located in the United States and substantially all product content is domestic. The Company’s firearms are sold through a select number of independent wholesale distributors principally to the commercial sporting market.

The Company manufactures and sells investment castings made from steel alloys for both outside customers and internal use in the firearms segment. Investment castings sold to outside customers, either directly to or through manufacturers’ representatives, represented 8% of the Company’s total sales for the year ended December 31, 2007.

#### Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### Revenue Recognition

Revenue is recognized, net of any estimated discounts, sales incentives, or rebates, when product is shipped and the customer takes ownership and assumes risk of loss.

#### Cash Equivalents

The Company considers interest-bearing deposits with financial institutions with remaining maturities of three months or less at the time of acquisition to be cash equivalents.

#### Short-term Investments

Short-term investments are recorded at cost plus accrued interest, which approximates market, and consist of a fund that invests principally in United States Treasury instruments, maturing within one year. The income from short-term investments is included in other income – net.

#### Accounts Receivable

Accounts receivable balances for significant customers follow:

| <i>As of December 31, (in thousands)</i> | <b>2007</b> | 2006    |
|--|-------------|---------|
| Customer 1                               | \$2,931     | \$ 727  |
| Customer 2                               | \$2,513     | \$1,318 |
| Customer 3                               | \$1,625     | \$1,763 |
| Customer 4                               | \$1,593     | \$2,203 |

The allowance for doubtful accounts and discounts was \$0.4 million in both 2007 and 2006.

The Company establishes an allowance for doubtful accounts based on the credit worthiness of its customers and historical experience. Bad debt expense has been immaterial during each of the last three years.

#### Inventories

Inventories are stated at the lower of cost, principally determined by the last-in, first-out (LIFO) method, or market. If inventories had been valued using the first-in, first-out method, inventory values would have been higher by approximately \$46.9 million and \$57.6 million at December 31, 2007 and 2006, respectively. During 2007 and 2006, inventory quantities were reduced. This reduction resulted in a liquidation of LIFO inventory quantities carried at lower costs prevailing in prior years as compared with the current cost of purchases, the effect of which decreased costs of products sold by approximately \$12.1 million and \$7.1 million in 2007 and 2006, respectively. There was no LIFO liquidation in 2005.

Inventories consist of the following:

| <i>As of December 31, (in thousands)</i> | <b>2007</b>     | 2006            |
|--|-----------------|-----------------|
| Finished products                        | \$ 1,859        | \$ 3,906        |
| Materials and products in process        | <u>11,438</u>   | <u>20,500</u>   |
| Net inventories                          | <u>\$13,297</u> | <u>\$24,406</u> |

#### Property, Plant, and Equipment

Property, plant, and equipment are stated on the basis of cost. Depreciation is computed using the straight-line and declining balance methods predominately over 15, 10, and 3 years for buildings, machinery and equipment, and tools and dies, respectively.

Property, plant and equipment consist of the following at cost:

| <i>As of December 31, (in thousands)</i> | <b>2007</b>      | 2006             |
|--|------------------|------------------|
| Land and improvements                    | \$ 1,194         | \$ 1,652         |
| Buildings and improvements               | 23,953           | 23,795           |
| Machinery and equipment                  | 83,173           | 86,155           |
| Dies and tools                           | <u>18,176</u>    | <u>16,440</u>    |
|  | <u>\$126,496</u> | <u>\$128,042</u> |

#### Long-lived Assets

Long-lived assets are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144. In performing this review, the carrying value of the assets is compared to the projected undiscounted cash flows to be generated from the assets. If the sum of the undiscounted expected future cash flows is less than the carrying value of the assets, the assets are considered to be impaired. Impairment losses are measured as the amount by which the carrying value of the assets exceeds the fair value of the assets. When fair value estimates are not available, the Company estimates fair value using the estimated future cash flows discounted at a rate commensurate with the risks associated with the recovery of the assets.

### Income Taxes

Income taxes are accounted for using the asset and liability method in accordance with SFAS No. 109. Under this method, deferred income taxes are recognized for the tax consequences of “temporary differences” by applying enacted statutory rates applicable to future years to temporary differences between the financial statement carrying amounts and the tax basis of the Company’s assets and liabilities.

### Product Liability

The Company provides for product liability claims including estimated legal costs to be incurred defending such claims. The provision for product liability claims is charged to cost of products sold.

### Advertising Costs

The Company expenses advertising costs as incurred. Advertising expenses for the years ended December 31, 2007, 2006, and 2005, were \$2.6 million, \$2.3 million, and \$2.0 million, respectively.

### Shipping Costs

Costs incurred related to the shipment of products are included in selling expense. Such costs totaled \$2.3 million, \$1.9 million, and \$1.9 million in 2007, 2006, and 2005, respectively.

### Stock Options

Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement 123(R), *Share-Based Payment*, utilizing the modified prospective approach. Prior to the adoption of SFAS 123(R) the Company accounted for stock option grants in accordance with APB Opinion 25, *Accounting for Stock Issued to Employees*, (the intrinsic value method), and accordingly, recognized no compensation expense for stock option grants.

Under the modified prospective approach, the provisions of SFAS 123(R) apply to new awards and to awards that were outstanding on January 1, 2006 that are subsequently modified, repurchased or cancelled. Under the modified prospective approach, compensation cost recognized includes compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). Prior periods were not restated to reflect the impact of adopting the new standard.

### Earnings Per Share

Basic earnings per share is based upon the weighted-average number of shares of Common Stock outstanding during the year, which was 22,441,700 in 2007, 25,775,400 in 2006 and 26,910,700 in 2005. Diluted earnings per share reflect the impact of options outstanding using the treasury stock method. This results in diluted weighted-average shares outstanding of 22,757,500 in 2007, 25,787,600 in 2006, and 26,910,700 in 2005.

### Reclassifications

Certain prior year balances may have been reclassified to conform with current year presentation.

## Recent Accounting Pronouncements

In September 2006, FASB issued FAS No. 157, “Fair Value Measurements” (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions of FAS 157 are effective for the fiscal year beginning January 1, 2008. The FASB has deferred the implementation of FAS 157 by one year for certain non-financial assets and liabilities such as this will be effective for the fiscal year beginning January 1, 2009. The adoption of FAS 157 is not expected to have a material impact on the Company’s financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), “Business Combinations” (“FAS 141R”). FAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquiree and the goodwill acquired. FAS 141R also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. FAS 141R is effective for the fiscal year beginning January 1, 2009, and will be adopted by the Company in the first quarter of 2009. The adoption of FAS 141R is not expected to have a material impact on the Company’s financial position, results of operations and cash flows.

## **2. Income Taxes**

The Federal and state income tax provision consisted of the following (in thousands):

| Year ended December 31, | 2007    |          | 2006    |           | 2005    |          |
|-------------------------|---------|----------|---------|-----------|---------|----------|
|                         | Current | Deferred | Current | Deferred  | Current | Deferred |
| Federal                 | \$3,782 | \$1,516  | \$2,587 | \$(1,925) | \$690   | \$(260)  |
| State                   | 687     | 345      | 739     | (662)     | 204     | (56)     |
|                         | \$4,469 | \$1,861  | \$3,326 | \$(2,587) | \$894   | \$(316)  |

Significant components of the Company's deferred tax assets and liabilities are as follows (in thousands):

| <i>December 31,</i>                            | <b>2007</b>    | 2006            |
|--|----------------|-----------------|
| Deferred tax assets:                           |                |                 |
| Product liability                              | \$734          | \$ 698          |
| Employee compensation and benefits             | 3,376          | 4,081           |
| Allowances for doubtful accounts and discounts | 143            | 458             |
| Inventories                                    | 1,675          | 2,674           |
| Additional minimum pension liability           | 8,205          | 8,289           |
| Asset impairment charges                       | 1,605          | 1,495           |
| Other  | 425            | 972             |
| <b>Total deferred tax assets</b>               | <b>16,163</b>  | <b>18,667</b>   |
| Deferred tax liabilities:                      |                |                 |
| Depreciation                                   | 796            | 1,030           |
| Pension plans                                  | 5,665          | 5,428           |
| Other  | 198            | 232             |
| <b>Total deferred tax liabilities</b>          | <b>6,659</b>   | <b>6,690</b>    |
| <b>Net deferred tax assets</b>                 | <b>\$9,504</b> | <b>\$11,977</b> |

In accordance with the provisions of SFAS No. 87, "Employers' Accounting for Pension Plan Costs," changes in deferred tax assets relating to the additional minimum pension liability are not charged to expense and are therefore not included in the deferred tax provision; instead they are charged to other comprehensive income.

The effective income tax rate varied from the statutory Federal income tax rate as follows:

| <i>Year ended December 31,</i>                 | <b>2007</b>  | 2006         | 2005         |
|--|--------------|--------------|--------------|
| Statutory Federal income tax rate              | 35.0%        | 34.0%        | 34.0%        |
| State income taxes, net of Federal tax benefit | 4.3          | 4.2          | 7.5          |
| Domestic production activities deduction       | (1.7)        | 0.2          | -            |
| Other items                                    | 0.4          | 1.7          | (1.4)        |
| <b>Effective income tax rate</b>               | <b>38.0%</b> | <b>40.1%</b> | <b>40.1%</b> |

The Company made income tax payments of approximately \$4.9 million, \$0.2 million, and \$3.1 million, during 2007, 2006, and 2005, respectively. The Company expects to realize its deferred tax assets through tax deductions against future taxable income or carry back against taxes previously paid.

The Company files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal and state income tax examinations by tax authorities for years before 2003. In the third quarter of 2007, the Internal Revenue Service (IRS) completed an examination of the Company's Federal income tax return for 2005. The IRS did not propose any adjustments as a result of this examination and has accepted the Company's return as filed.

The Company adopted the provisions of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," on January 1, 2007. Upon the adoption of FIN 48, the Company commenced a review

of all open tax years in all jurisdictions. The Company does not believe it has included any “uncertain tax positions” in its Federal income tax return or any of the state income tax returns it is currently filing. The Company has made an evaluation of the potential impact of additional state taxes being assessed by jurisdictions in which the Company does not currently consider itself liable. The Company does not anticipate that such additional taxes, if any, would result in a material change to its financial position. However, the Company anticipates that it is more likely than not that additional state tax liabilities in the range of \$0.4 to \$0.7 million exist. The Company had previously recorded \$0.4 million relating to these additional state income taxes, including approximately \$0.2 million for the payment of interest and penalties. This amount is included in income taxes payable at December 31, 2007. In connection with the adoption of FIN 48, the Company will include interest and penalties related to uncertain tax positions as a component of its provision for taxes.

### 3. Pension Plans

The Company sponsors two defined benefit pension plans that cover substantially all employees. A third defined benefit pension plan is non-qualified and covers certain executive officers of the Company.

The cost of these defined benefit plans and the balances of plan assets and obligations are as follows (in thousands):

| <b>Change in Benefit Obligation</b>             | <b>2007</b>     | <b>2006</b>     |
|---|-----------------|-----------------|
| Benefit obligation at January 1                 | \$64,167        | \$64,481        |
| Service cost                                    | 1,590           | 1,670           |
| Interest cost                                   | 3,672           | 3,444           |
| Actuarial loss (gain)                           | 4,090           | (3,051)         |
| Benefits paid                                   | (2,609)         | (2,377)         |
| Curtailments                                    | (2,236)         | -               |
| <b>Benefit obligation at December 31</b>        | <b>68,674</b>   | <b>64,167</b>   |
| <b>Change in Plan Assets</b>                    |                 |                 |
| Fair value of plan assets at January 1          | 56,527          | 53,206          |
| Actual return on plan assets                    | 3,057           | 3,463           |
| Employer contributions                          | 6,859           | 2,236           |
| Benefits paid                                   | (2,609)         | (2,378)         |
| <b>Fair value of plan assets at December 31</b> | <b>63,834</b>   | <b>56,527</b>   |
| <i>Funded Status</i>                            |                 |                 |
| Funded status                                   | (4,840)         | (7,640)         |
| Unrecognized net actuarial loss                 | 21,575          | 19,398          |
| Unrecognized prior service cost                 | 20              | 1,324           |
| Unrecognized transition obligation (asset)      | -               | -               |
| <b>Net amount recognized</b>                    | <b>\$16,755</b> | <b>\$13,082</b> |



| <i>Weighted Average Assumptions for the years ended December 31,</i> | <b>2007</b> | 2006  |
|--|-------------|-------|
| Discount rate  | 5.75%       | 5.50% |
| Expected long-term return on plan assets                             | 8.00%       | 8.00% |
| Rate of compensation increases                                       | 5.00%       | 5.00% |

**Components of Net Periodic Pension Cost**

|                                 |         |         |
|---------------------------------|---------|---------|
| Service cost                    | \$1,590 | \$1,670 |
| Interest cost                   | 3,672   | 3,444   |
| Expected return on assets       | (4,488) | (4,235) |
| Recognized gains                | 1,108   | 1,243   |
| Prior service cost recognized   | 161     | 161     |
| Net periodic pension cost       | \$2,043 | \$2,283 |
| Pension plan curtailment        | 1,143   | -       |
| Total net periodic pension cost | \$3,186 | \$2,283 |

**Amounts Recognized on the Balance Sheet**

|  | <b>2007</b> | 2006      |
|--|-------------|-----------|
| Accrued benefit liability                          | \$(4,839)   | \$(7,640) |
| Accumulated other comprehensive income, net of tax | 13,389      | 12,433    |
| Deferred tax asset                                 | 8,205       | 8,289     |
|  | \$16,755    | \$13,082  |

| <i>Weighted Average Assumptions as of December 31,</i> | <b>2007</b> | 2006  |
|--|-------------|-------|
| Discount rate  | 5.75%       | 5.75% |
| Rate of compensation increases                         | 5.00%       | 5.00% |

*Information for Pension Plans with an Accumulated Benefit Obligation in excess of plan assets*

|                                | <b>2007</b> | 2006     |
|--------------------------------|-------------|----------|
| Projected benefit obligation   | \$68,674    | \$64,167 |
| Accumulated benefit obligation | \$68,708    | \$62,284 |
| Fair value of plan assets      | \$63,834    | \$56,527 |

*Pension Weighted Average Asset Allocations as of December 31,*

|                    | <b>2007</b> | 2006 |
|--------------------|-------------|------|
| Debt securities    | 40%         | 70%  |
| Equity securities  | 53%         | 27%  |
| Real estate        | 4%          | -    |
| Money market funds | 3%          | 3%   |
|                    | 100%        | 100% |

The estimated future benefit payments for the defined benefit plans, which reflect future service as appropriate, for each of the next five years and the total amount for years six through ten, are as follows: 2008-\$2.8 million, 2009-\$3.0 million, 2010-\$3.1 million, 2011-\$3.3 million, 2012-\$3.5 million, and for the five year period ending 2017-\$21.5 million.

The accumulated benefit obligation for all the defined benefit pension plans was \$68.7 million and \$62.3 million as of December 31, 2007 and 2006, respectively.

The measurement dates of the assets and liabilities of all plans presented for 2007 and 2006 were December 31, 2007 and December 31, 2006, respectively.

The current investment objective is to produce income and long-term appreciation through a target asset allocation of 35% debt securities and other fixed income investments including cash and short-term instruments, and 65% equity investments, to provide for the current and future benefit payments of the plans. The previous investment objective had a target allocation of 65% debt securities and other fixed income investments including cash and short-term instruments, and 35% equity investments. The asset allocation is being converted to the current target asset allocation over an 18-month period. The pension plans are not invested in the common stock of the Company.

The Company determines the expected return on plan assets based on the target asset allocations. In addition, the historical returns of the plan assets are also considered in arriving at the expected rate of return.

In accordance with SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" and its predecessor, SFAS No. 87, "Employers' Accounting for Pension Costs", the Company recorded an additional minimum pension liability, net of tax, which decreased comprehensive income by \$0.5 million, \$0.3 million, and \$1.9 million, in 2007, 2006, and 2005, respectively.

In prior years, the Company also sponsored two defined contribution plans which covered substantially all of its hourly and salaried employees and a non-qualified defined contribution plan which covers certain of its salaried employees. Expenses related to the defined contribution plans were \$1.1 million and \$1.5 million in 2006, and 2005, respectively.

Effective January 1, 2007, all qualified and non-qualified defined contribution plans were merged into a single 401(k) plan. Under the terms of the 401(k) plan, the Company matched a certain portion of employee contributions effective January 1, 2007. Expenses related to the 401(k) plan were \$0.8 million in 2007.

In 2007, the Company amended its hourly and salaried defined benefit pension plans so that employees will no longer accrue benefits under these plans effective December 31, 2007. This action "freezes" the benefits for all employees and prevents future hires from joining the plans, effective December 31, 2007. Starting in 2008, the Company will provide supplemental discretionary contributions to substantially all employees' individual 401(k) accounts.

These amendments resulted in a \$1.1 million pension curtailment charge that was recognized in 2007.

In 2008 and future years, the Company will likely be required to make cash contributions to the two defined benefit pension plans according to the new rules of the Pension Protection Act of 2006. The annual contributions will be based on the amount of the unfunded plan liabilities derived from the frozen benefits and will not include liabilities for any future accrued benefits for any new or existing participants. The total amount of these future cash contributions will be dependent on the investment returns generated by the plans' assets and the then-applicable discount rates used to calculate the plans' liabilities. The 2008 cash contribution for the defined benefit plans is not expected to exceed \$1 million.

In future years, the total annual cash outlays for retirement benefits, which would include the continuing funding of the two defined benefit pension plans and the new supplemental discretionary 401(k) contributions, are expected to be comparable to the current retirement funding levels.

In February 2008, the Company made lump sum benefit payments to two participants in its only non-qualified defined benefit plan, the Supplemental Executive Retirement Plan (SERP). These payments, which totaled \$2.1 million, represented the actuarial present value of the participants' accrued benefit as of the date of payment. Only one, retired participant remains in this plan.

FAS No. 158 requires an employer to measure the funded status of a plan as of its year-end date and was first effective for fiscal 2006 for the Company. Upon adoption of this standard in 2006, the Company recorded a charge of \$1.6 million, net of tax, to other comprehensive income and a \$2.6 million credit to accrued pension liability.

#### **4. Line of Credit**

In December 2007, the Company secured a \$25 million credit facility with a bank which terminates on December 13, 2008. Borrowings under this facility bear interest at LIBOR plus 100 basis points. At December 31, 2007, the Company was in compliance with the terms and covenants of the credit agreement. The unused fee is 25 basis points per year on the unused portion of the credit facility. This credit facility remains unused at December 31, 2007.

#### **5. Stock Incentive and Bonus Plans**

In 1998, the Company adopted, and in May 1999 the shareholders approved, the 1998 Stock Incentive Plan (the "1998 Plan") under which employees were granted options to purchase shares of the Company's Common Stock and stock appreciation rights. The Company reserved 2,000,000 shares for issuance under the 1998 Plan. These options have an exercise price equal to the fair market value of the shares of the Company at the date of grant, become vested ratably over five years, and expire ten years from the date of grant. In April 2007, all reserved shares for which a stock option had not been granted under the 1998 Plan were deregistered. No further stock options or stock will be granted under the 1998 Plan.

On December 18, 2000, the Company adopted, and in May 2001 the shareholders approved, the 2001 Stock Option Plan for Non-Employee Directors (the "2001 Plan") under which non-employee directors were granted options to purchase shares of the Company's authorized but unissued stock. The Company reserved 200,000 shares for issuance under the 2001 Plan. Options granted under the 2001 Plan have an exercise price equal to the fair market value of the shares of the Company at the date of grant and expire ten years from the date of grant. Twenty-five percent of the options vest immediately upon grant and the remaining options vest ratably over three years. In April 2007, all reserved shares for which a stock

option had not been granted under the 2001 Plan were deregistered. No further stock options or stock will be granted under the 2001 Plan.

In April 2007, the Company adopted and the shareholders approved the 2007 Stock Incentive Plan (2007 SIP) under which employees, independent contractors, and non-employee directors may be granted stock options, restricted stock, deferred stock awards, and stock appreciation rights, any of which may or may not require the satisfaction of performance objectives. Vesting requirements will be determined by the Compensation Committee or the Board of Directors. The Company has reserved 2,550,000 shares for issuance under the 2007 SIP.

In 2007, a total of 10,920 deferred stock awards were issued to non-employee directors, which will vest in April 2008. Compensation expense related to these awards are amortized ratably over the vesting period. The total compensation expense related to these awards is \$0.1 million. The impact on the 2008 results will be immaterial.

In 2007, a total of 29,500 shares of stock were awarded to employees. All compensation expense related to these awards, which totaled \$0.4 million, was recognized in 2007.

The following table summarizes the stock option activity of the Plans:

|   | Shares    | Weighted Avg<br>Exercise Price | Weighted Avg<br>Grant Date<br>Fair Value | Weighted Avg<br>Remaining<br>Contractual<br>Life (Years) |
|---|-----------|--------------------------------|--|--|
| Outstanding at December 31, 2004                        | 1,095,000 | 11.55                          | 1.86                                     | 4.3  |
| Granted   | 40,000    | 10.88                          | 2.24                                     | 9.5  |
| Exercised   | -         | -                              | -  | -  |
| Canceled  | (115,000) | 11.74                          | 1.83                                     | 3.2  |
| Outstanding at December 31, 2005                        | 1,020,000 | 11.50                          | 1.89                                     | 3.3  |
| Granted   | 660,000   | 8.51                           | 3.51                                     | 9.7  |
| Exercised   | -         | -                              | -  | -  |
| Canceled  | (355,000) | 11.90                          | 2.00                                     | 2.3  |
| Outstanding at December 31, 2006                        | 1,325,000 | 9.46                           | 2.66                                     | 5.4  |
| Granted   | 311,250   | 13.06                          | 5.67                                     | 9.3  |
| Exercised   | (495,000) | 11.77                          | 1.92                                     | 1.2  |
| Canceled  | (50,000)  | 9.59                           | 1.24                                     | 3.5  |
| Outstanding at December 31, 2007                        | 1,091,250 | 9.44                           | 3.91                                     | 8.4  |
| Exercisable Options Outstanding at<br>December 31, 2007 | 265,000   | 8.55                           | 2.59                                     | 6.5  |
| Non-Vested Options Outstanding at<br>December 31, 2007  | 826,250   | 9.72                           | 4.33                                     | 9.0  |

At December 31, 2007, an aggregate of 2,238,750 shares remain available for grant under the Plans.

The Company uses the Black-Scholes option pricing model to estimate the fair value of stock-based awards with the following weighted average assumptions:

|                          | 2007      | 2006    | 2005    |
|--------------------------|-----------|---------|---------|
| Dividend yield           | 0.0%      | 0.0%    | 0.0%    |
| Expected volatility      | 33.9%     | 44.3%   | 44.3%   |
| Risk free rate of return | 4.0%      | 4.0%    | 4.0%    |
| Expected lives           | 7.5 years | 5 years | 5 years |

The estimated fair value of options granted is subject to the assumptions made and if the assumptions changed, the estimated fair value amounts could be significantly different.

As a result of adopting Statement 123(R) on January 1, 2006, the Company's income before income taxes and net income for the years ended December 31, 2007 and 2006 are \$0.8 million and \$0.5 million and \$0.2 million and \$0.1 million lower, respectively, than if it had continued to account for share-based compensation under Opinion 25 for stock option grants. Basic and diluted earnings per share were unchanged. If the Company would have adopted Statement 123(R) for the year ended December 31, 2005, the impact on the Company's income before income taxes and net income for that year would have been insignificant.

At December 31, 2007, there was \$1.9 million of unrecognized compensation cost related to share-based payments that is expected to be recognized over a weighted-average period of 2.3 years.

At December 31, 2007 the aggregate intrinsic value of all options, including exercisable options, was \$4.3 million.

## **6. Contingent Liabilities**

As of December 31, 2007, the Company is a defendant in approximately 5 lawsuits involving its products and is aware of certain other such claims. These lawsuits and claims fall into two categories:

- (i) those that claim damages from the Company related to allegedly defective product design which stem from a specific incident. Pending lawsuits and claims are based principally on the theory of "strict liability" but also may be based on negligence, breach of warranty, and other legal theories; and
- (ii) those brought by cities or other governmental entities, and individuals against firearms manufacturers, distributors and dealers seeking to recover damages allegedly arising out of the misuse of firearms by third parties in the commission of homicides, suicides and other shootings involving juveniles and adults. The complaints by municipalities seek damages, among other things, for the costs of medical care, police and emergency services, public health services, and the maintenance of courts, prisons, and other services. In certain instances, the plaintiffs seek to recover for decreases in property values and loss of business within the city due to criminal violence. In addition, nuisance abatement and/or injunctive relief is sought to change the design, manufacture, marketing and distribution practices of the various defendants. These suits allege, among other claims, strict liability or negligence in the design of products, public nuisance, negligent entrustment, negligent distribution, deceptive

or fraudulent advertising, violation of consumer protection statutes and conspiracy or concert of action theories. Most of these cases do not allege a specific injury to a specific individual as a result of the misuse or use of any of the Company's products.

The Company has expended significant amounts of financial resources and management time in connection with product liability litigation. Management believes that, in every case involving firearms, the allegations are unfounded, and that the shootings and any results therefrom were due to negligence or misuse of the firearms by third-parties or the claimant, and that there should be no recovery against the Company. Defenses further exist to the suits brought by governmental entities based, among other reasons, on established state law precluding recovery for essential government services, the remoteness of the claims, the types of damages sought to be recovered, and limitations on the extraterritorial authority which may be exerted by a city, municipality, county or state under state and federal law, including State and Federal Constitutions.

The only case against the Company alleging liability for criminal shootings by third-parties to ever be permitted to go before a constitutional jury, Hamilton, et al. v. Accu-tek, et al., resulted in a defense verdict in favor of the Company on February 11, 1999. In that case, numerous firearms manufacturers and distributors had been sued, alleging damages as a result of alleged negligent sales practices and "industry-wide" liability. The Company and its marketing and distribution practices were exonerated from any claims of negligence in each of the seven cases decided by the jury. In subsequent proceedings involving other defendants, the New York Court of Appeals as a matter of law confirmed that 1) no legal duty existed under the circumstances to prevent or investigate criminal misuses of a manufacturer's lawfully made products; and 2) liability of firearms manufacturers could not be apportioned under a market share theory. More recently, the New York Court of Appeals on October 21, 2003 declined to hear the appeal from the decision of the New York Supreme Court, Appellate Division, affirming the dismissal of New York Attorney General Eliot Spitzer's public nuisance suit against the Company and other manufacturers and distributors of firearms. In its decision, the Appellate Division relied heavily on Hamilton in concluding that it was "legally inappropriate," "impractical," "unrealistic" and "unfair" to attempt to hold firearms manufacturers responsible under theories of public nuisance for the criminal acts of others.

Of the lawsuits brought by municipalities, counties or a state Attorney General, twenty have been concluded: Atlanta – dismissal by intermediate Appellate Court, no further appeal; Bridgeport – dismissal affirmed by Connecticut Supreme Court; County of Camden – dismissal affirmed by U.S. Third Circuit Court of Appeals; Miami – dismissal affirmed by intermediate appellate court, Florida Supreme Court declined review; New Orleans – dismissed by Louisiana Supreme Court, United States Supreme Court declined review; Philadelphia – U.S. Third Circuit Court of Appeals affirmed dismissal, no further appeal; Wilmington – dismissed by trial court, no appeal; Boston – voluntary dismissal with prejudice by the City at the close of fact discovery; Cincinnati – voluntarily withdrawn after a unanimous vote of the city council; Detroit – dismissed by Michigan Court of Appeals, no appeal; Wayne County – dismissed by Michigan Court of Appeals, no appeal; New York State – Court of Appeals denied plaintiff's petition for leave to appeal the Intermediate Appellate Court's dismissal, no further appeal; Newark – Superior Court of New Jersey Law Division for Essex County dismissed the case with prejudice; City of Camden – dismissed on July 7, 2003, not reopened; Jersey City – voluntarily dismissed and not re-filed; St. Louis – Missouri Supreme Court denied plaintiffs' motion to appeal Missouri Appellate Court's affirmation of dismissal; Chicago – Illinois Supreme Court affirmed trial court's dismissal; and Los Angeles City, Los Angeles County, San Francisco – Appellate Court

affirmed summary judgment in favor of defendants, no further appeal; and Cleveland – dismissed on January 24, 2006 for lack of prosecution.

The dismissal of the Washington, D.C. municipal lawsuit was sustained on appeal, but individual plaintiffs were permitted to proceed to discovery and attempt to identify the manufacturers of the firearms used in their shootings as “machine guns” under the city’s “strict liability” law. On April 21, 2005, the D.C. Court of Appeals, in an *en banc* hearing, unanimously dismissed all negligence and public nuisance claims, but let stand individual claims based upon a Washington, D.C. act imposing “strict liability” for manufacturers of “machine guns.” Based on present information, none of the Company’s products has been identified with any of the criminal assaults which form the basis of the individual claims. The writ of certiorari to the United States Supreme Court regarding the constitutionality of the Washington, D.C. act was denied and the case was remanded to the trial court for further proceedings. The defendants subsequently moved to dismiss the case based upon the Protection of Lawful Commerce in Arms Act, which motion was granted on May 22, 2006. The individual plaintiffs and the District of Columbia, which has subrogation claims in regard to the individual plaintiffs, appealed. On January 10, 2008, the District of Columbia Court of Appeals unanimously upheld the dismissal. Plaintiffs have until February 25, 2008, to move for rehearing *en banc*.

The Indiana Court of Appeals affirmed the dismissal of the Gary case by the trial court, but the Indiana Supreme Court reversed this dismissal and remanded the case for discovery proceedings on December 23, 2003. Gary is scheduled to begin trial in 2009. The defendants filed a motion to dismiss pursuant to the Protection of Lawful Commerce in Arms Act (“PLCAA”). The state court judge held the PLCAA unconstitutional and the defendants filed a motion with the Indiana Court of Appeals asking it to accept interlocutory appeal on the issue, which appeal was accepted on February 5, 2007. On October 29, 2007, the Indiana Appellate Court affirmed, holding that the PLCAA does not apply to the City’s claims. A petition for rehearing was filed in the Appellate Court and denied on January 9, 2008. A Petition to Transfer the appeal to the Supreme Court of Indiana was filed on February 7, 2008.

In the previously reported New York City municipal case, the defendants moved to dismiss the suit pursuant to the Protection of Lawful Commerce in Arms Act. The trial judge found the Act to be constitutional but denied the defendants’ motion to dismiss the case, stating that the Act was not applicable to the suit. The defendants were given leave to appeal and in fact have appealed the decision to the U.S. Court of Appeals for the Second Circuit. That appeal remains pending.

In the NAACP case, on May 14, 2003, an advisory jury returned a verdict rejecting the NAACP’s claims. On July 21, 2003, Judge Jack B. Weinstein entered an order dismissing the NAACP lawsuit, but this order contained lengthy dicta which defendants believe are contrary to law and fact. Appeals by both sides were filed, but plaintiffs withdrew their appeal. On August 3, 2004, the United States Court of Appeals for the Second Circuit granted the NAACP’s motion to dismiss the defendants’ appeal of Judge Weinstein’s order denying defendants’ motion to strike his dicta made in his order dismissing the NAACP’s case, and the defendants’ motion for summary disposition was denied as moot. The ruling of the Second Circuit effectively confirmed the decision in favor of defendants and brought this matter to a conclusion.

Legislation has been passed in approximately 34 states precluding suits of the type brought by the municipalities mentioned above. On the Federal level, the “Protection of Lawful Commerce in Arms Act” was signed by President Bush on October 26, 2005. The Act requires dismissal of suits against manufacturers arising out of the lawful sale of their products for harm resulting from the criminal or

unlawful misuse of a firearm by a third party. The Company is pursuing dismissal of each action involving such claims, including the municipal cases described above. The Company was voluntarily dismissed with prejudice on March 23, 2007 from the previously reported Arnold case. The matter was thus concluded with no payment by the Company.

Punitive damages, as well as compensatory damages, are demanded in certain of the lawsuits and claims. Aggregate claimed amounts presently exceed product liability accruals and applicable insurance coverage. For claims made after July 10, 2000, coverage is provided on an annual basis for losses exceeding \$5 million per claim, or an aggregate maximum loss of \$10 million annually, except for certain new claims which might be brought by governments or municipalities after July 10, 2000, which are excluded from coverage.

Product liability claim payments are made when appropriate if, as, and when claimants and the Company reach agreement upon an amount to finally resolve all claims. Legal costs are paid as the lawsuits and claims develop, the timing of which may vary greatly from case to case. A time schedule cannot be determined in advance with any reliability concerning when payments will be made in any given case.

Provision is made for product liability claims based upon many factors related to the severity of the alleged injury and potential liability exposure, based upon prior claim experience. Because our experience in defending these lawsuits and claims is that unfavorable outcomes are typically not probable or estimable, only in rare cases is an accrual established for such costs. In most cases, an accrual is established only for estimated legal defense costs. Product liability accruals are periodically reviewed to reflect then-current estimates of possible liabilities and expenses incurred to date and reasonably anticipated in the future. Threatened product liability claims are reflected in our product liability accrual on the same basis as actual claims; i.e., an accrual is made for reasonably anticipated possible liability and claims-handling expenses on an ongoing basis.

A range of reasonably possible loss relating to unfavorable outcomes cannot be made. However, in product liability cases in which a dollar amount of damages is claimed, the amount of damages claimed, which totaled \$5 million and \$0 at December 31, 2007 and 2006, respectively, are set forth as an indication of possible maximum liability that the Company might be required to incur in these cases (regardless of the likelihood or reasonable probability of any or all of this amount being awarded to claimants) as a result of adverse judgments that are sustained on appeal.

As of December 31, 2007 and 2006, the Company was a defendant in 5 and 4 lawsuits, respectively, involving its products and is aware of other such claims. During the year ended December 31, 2007 and 2006, respectively, 2 and 2 claims were filed against the Company, 1 and 2 claims were dismissed, and 0 and 2 claims were settled. The average cost per settled claim was \$47,000 in 2006.

During the years ended December 31, 2007 and 2006, the Company incurred product liability expense of \$1.7 million and \$2.5 million, respectively, which includes the cost of outside legal fees, insurance, and other expenses incurred in the management and defense of product liability matters.

The Company management monitors the status of known claims and the product liability accrual, which includes amounts for asserted and unasserted claims. While it is not possible to forecast the outcome of litigation or the timing of costs, in the opinion of management, after consultation with special and corporate counsel, it is not probable and is unlikely that litigation, including punitive damage claims,



will have a material adverse effect on the financial position of the Company, but may have a material impact on the Company's financial results for a particular period.

The Company has reported all cases instituted against it through September 30, 2007 and the results of those cases, where terminated, to the S.E.C. on its previous Form 10-K and 10-Q reports, to which reference is hereby made.

### Balance Sheet Rollforward for Product Liability Reserve

(Dollars in thousands)

|      | Balance<br>Beginning<br>of Year (a) | Accrued<br>Legal<br>Expense<br>(b) | Cash Payments     |                    |                       |                   | Balance<br>End of<br>Year (a) |
|------|-------------------------------------|------------------------------------|-------------------|--------------------|-----------------------|-------------------|-------------------------------|
|      |                                     |                                    | Legal Fees<br>(c) | Settlements<br>(d) | Insurance<br>Premiums | Admin.<br>Expense |                               |
| 2005 | \$3,132                             | \$2,514                            | \$(2,935)         | (515)              | N/A                   | N/A               | \$2,196                       |
| 2006 | 2,196                               | 688                                | (1,000)           | (143)              | N/A                   | N/A               | 1,741                         |
| 2007 | 1,741                               | 639                                | (447)             | -                  | N/A                   | N/A               | 1,933                         |

### Income Statement Detail for Product Liability Expense

(Dollars in thousands)

|      | Accrued<br>Legal<br>Expense<br>(b) | Insurance<br>Premium<br>Expense<br>(e) | Admin.<br>Expense<br>(f) | Total<br>Product<br>Liability<br>Expense |
|------|------------------------------------|--|--------------------------|--|
| 2005 | \$2,514                            | \$1,338                                | \$1,041                  | \$4,893                                  |
| 2006 | 688                                | 1,141                                  | 691                      | 2,520                                    |
| 2007 | 639                                | 748                                    | 299                      | 1,686                                    |

### Notes

- (a) The beginning and ending liability balances represent accrued legal fees only. Settlements and administrative costs are expensed as incurred. Only in rare instances is an accrual established for settlements.
- (b) The expense accrued in the liability is for legal fees only.
- (c) Legal fees represent payments to outside counsel related to product liability matters.
- (d) Settlements represent payments made to plaintiffs or allegedly injured parties in exchange for a full and complete release of liability.

- (e) Insurance expense represents the cost of insurance premiums.
- (f) Administrative expense represents personnel related and travel expenses of Company employees and firearm experts related to the management and monitoring of product liability matters.

There were no insurance recoveries during any of the above years.

## **7. Asset Impairment Charges**

In 2007, 2006 and 2005 the Company recognized asset impairment charges of \$2.3 million, \$0.5 million and \$0.5 million, respectively, related to certain assets in the corporate and investment castings segments. The Company was required to reduce the carrying value of these assets to fair value and recognized asset impairment charges because the carrying value of the affected assets exceeded their projected future undiscounted cash flows.

## **8. Stock Repurchase**

On January 26, 2007, the Company announced that its Board of Directors authorized a stock repurchase program. During the fourth quarter of 2007, the Company repurchased 2,216,000 shares of its common stock, representing 9.7% of the outstanding shares, on the open market at an average price of \$8.99 per share. On September 26, 2006, the Company repurchased 4,272,000 shares of its common stock, representing 15.9% of the outstanding shares, from entities controlled by members of the Ruger family at a price of \$5.90 per share. These purchases were made with cash held by the Company and no debt was incurred.

## **9. Related Party Transactions**

In February 2008, the Company made a lump sum pension benefit payment to William B. Ruger, Jr., the former Chairman and Chief Executive Officer of the Company. This payment totaled \$1.1 million which represented the actuarially determined present value of Mr. Ruger's accrued benefit as of the date of payment.

In March 2007 the Company sold 42 parcels of non-manufacturing real property held for investment for \$7.3 million to William B. Ruger, the Company's former Chief Executive Officer and Chairman of the Board. The sales price was based upon an independent appraisal. The sale included substantially all of the Company's raw land non-manufacturing real property assets in New Hampshire. The Company recognized a gain of \$5.2 million on the sale. Also in March 2007, the Company sold several pieces of artwork to members of the Ruger family for \$0.1 million and recognized insignificant gains from these sales.

In 2006 and 2005, the Company paid Newport Mills, \$9,800 and \$205,500, respectively, for storage rental and office space. The sole proprietor of Newport Mills is William B. Ruger, Jr. who was Chairman and Chief Executive Officer of the Company at the time. As of December 31, 2006, the Company no longer occupied this storage and office space. On December 16, 2005, the Company sold two automobiles to Mr. Ruger, Jr. for \$15,000.

## **10. Operating Segment Information**

The Company has two reportable operating segments: firearms and investment castings. The firearms segment manufactures and sells rifles, pistols, revolvers, and shotguns principally to a select number of licensed independent wholesale distributors primarily located in the United States. The investment castings segment manufactures and sells steel investment castings.

Corporate segment income relates to interest income on short-term investments, the sale of non-operating assets, and other non-operating activities. Corporate segment assets consist of cash and short-term investments and other non-operating assets.

The Company evaluates performance and allocates resources, in part, based on profit and loss before taxes. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies (see Note 1). Intersegment sales are recorded at the Company's cost plus a fixed profit percentage.

The Company's assets are located entirely in the United States and domestic sales represent at least 95% of total sales in 2007, 2006, and 2005.

Revenues from significant customers in 2007, 2006, and 2005 were as follows:

| <i>Year ended December 31, (in thousands)</i> | <b>2007</b> | 2006      | 2005      |
|---|-------------|-----------|-----------|
| Customer 1                                    | \$18,500    | \$18,600  | \$12,700  |
| Customer 2                                    | 16,900      | 18,100    | 21,600    |
| Customer 3                                    | 17,200      | 17,400    | 16,500    |
| Customer 4                                    | 13,700      | 12,300    | 13,800    |
| Customer 5                                    | 10,000      | 10,500    | 15,900    |
| <hr/>   |             |           |           |
| <i>Year ended December 31, (in thousands)</i> | <b>2007</b> | 2006      | 2005      |
| <b>Net Sales</b>                              |             |           |           |
| Firearms                                      | \$144,222   | \$139,110 | \$132,805 |
| Castings                                      |             |           |           |
| Unaffiliated                                  | 12,263      | 28,510    | 21,917    |
| Intersegment                                  | 9,165       | 11,818    | 18,045    |
|   | 21,428      | 40,328    | 39,962    |
| Eliminations                                  | (9,165)     | (11,818)  | (18,045)  |
|   | \$156,485   | \$167,620 | \$154,722 |
| <hr/>   |             |           |           |
| <b>Income (Loss) Before Income Taxes</b>      |             |           |           |
| Firearms                                      | \$11,400    | \$ 1,387  | \$ 2,524  |
| Castings                                      | (2,806)     | (1,178)   | (1,711)   |
| Corporate                                     | 8,065       | 1,634     | 629       |
|   | \$16,659    | \$ 1,843  | \$ 1,442  |
| <hr/>   |             |           |           |
| <b>Identifiable Assets</b>                    |             |           |           |
| Firearms                                      | \$47,870    | \$ 53,525 | \$ 73,035 |
| Castings                                      | 6,165       | 17,154    | 17,751    |
| Corporate                                     | 47,847      | 46,387    | 48,853    |
|   | 101,882     | \$117,066 | \$139,639 |
| <hr/>   |             |           |           |
| <b>Depreciation</b>                           |             |           |           |
| Firearms                                      | \$3,563     | \$ 2,475  | \$ 3,759  |
| Castings                                      | 809         | 1,377     | 1,681     |
|   | \$4,372     | \$ 3,852  | \$ 5,440  |
| <hr/>   |             |           |           |
| <b>Capital Expenditures</b>                   |             |           |           |
| Firearms                                      | \$3,950     | \$ 3,486  | \$ 3,116  |
| Castings                                      | 518         | 420       | 1,344     |
|   | \$4,468     | \$ 3,906  | \$ 4,460  |

## 12. Quarterly Results of Operations (Unaudited)

The following is a tabulation of the unaudited quarterly results of operations for the two years ended December 31, 2007 (in thousands, except per share data):

|                                   | Three Months Ended |          |          |          |
|-----------------------------------|--------------------|----------|----------|----------|
|                                   | 3/31/07            | 6/30/07  | 9/30/07  | 12/31/07 |
| Net Sales                         | \$48,456           | \$42,107 | \$31,863 | \$34,058 |
| Gross profit                      | 15,563             | 13,128   | 5,595    | 5,012    |
| Net income (loss)                 | 8,060              | 5,131    | (617)    | (2,245)  |
| Basic earnings (loss) per share   | 0.36               | 0.23     | (0.03)   | (0.10)   |
| Diluted earnings (loss) per share | 0.36               | 0.22     | (0.03)   | (0.10)   |

|   | Three Months Ended |          |          |          |
|---|--------------------|----------|----------|----------|
|   | 3/31/06            | 6/30/06  | 9/30/06  | 12/31/06 |
| Net Sales                                   | \$47,427           | \$35,276 | \$41,612 | \$43,305 |
| Gross profit                                | 10,023             | 8,385    | 6,199    | 3,403    |
| Net income (loss)                           | 1,419              | 1,448    | 957      | (2,720)  |
| Basic and diluted earnings (loss) per share | 0.05               | 0.06     | 0.04     | (0.11)   |

In the fourth quarter of 2007, the Company recorded an asset impairment charge of \$1.8 million related to the Dorr Building, a non-manufacturing property in New Hampshire that has been for sale for an extended period of time without any meaningful market interest.

In the fourth quarter of 2006, a \$2.5 million non-cash inventory valuation adjustment, net of the LIFO impact, was recorded to recognize inefficiencies in labor and overhead during a period of rapid inventory reduction. This over-absorption of labor and overhead was quantified by a physical inventory taken in the fourth quarter.

Due to the timing of the physical inventory, the Company was unable to quantify the impact of this delayed recognition of labor and overhead inefficiencies, if any, on the financial results of prior quarters. As a consequence, raw material and work in process physical inventories are being performed at the end of each quarter until a permanent corrective action is established and determined to be adequate, making these physical inventories unnecessary. These physical inventories were taken each quarter in 2007 and are expected to continue in 2008.

### 13. Other Operating Expenses (Income), net

Other net operating expenses (income) consist of the following:

| Year ended December 31,                      | 2007     | 2006    | 2005 |
|--|----------|---------|------|
| Gain on sale of operating assets (a)         | \$ (472) | \$(929) | -    |
| Impairment of operating assets (b)           | 489      | 494     | 483  |
| Gain on sale of real estate (c)              | (1,521)  | (397)   | -    |
| Impairment of real estate held for sale (d)  | 1,775    | -       | -    |
| Total other operating expenses (income), net | \$ 271   | \$(832) | 483  |

(a) The gain on sale of operating assets was generated primarily from the sale of used machinery and equipment. Most of the used machinery and equipment sold in 2007 and 2006 was related to titanium investment casting.

(b) In 2007, the Company recognized an impairment charge of \$0.5 million related to machinery and equipment previously in the Company's Arizona investment casting operations. In 2006, the Company recognized an impairment charge of \$0.5 million related to building improvements at the Dorr Building. The Company had planned to establish a titanium investment castings foundry at Dorr, but that plan was aborted in 2006.

(c) On April 16, 2007, the Company sold a non-manufacturing facility in Arizona for \$5.0 million. This facility had not been used in the Company's operations for several years. The Company realized a gain of approximately \$1.5 million from this sale. In 2006, the \$0.4 million gain on sale of real estate reflects the sale of non-manufacturing real property. The Company has three additional non-manufacturing properties listed for sale, two in Connecticut and one in New Hampshire.

(d) In late 2007, the Company recognized an asset impairment charge of \$1.8 million related to the Dorr Building, a non-manufacturing property in New Hampshire that has been for sale for an extended period of time without any meaningful market interest.

## **ITEM 9—CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

## **ITEM 9A—CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

The Company conducted an evaluation, with the participation of its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of December 31, 2007. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that as of December 31, 2007, the Company's controls and procedures over financial reporting were effective.

### **Management's Report on Internal Control over Financial Reporting**

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company conducted an evaluation, with the participation of its Chief Executive Officer and Chief Financial Officer, of the effectiveness of its internal control over financial reporting as of December 31, 2007. This evaluation was performed based on the framework in "Internal Control — Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

Management has concluded that the Company maintained effective internal control over financial reporting as of December 31, 2007, based on criteria established in "Internal Control — Integrated Framework" issued by the COSO.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2007 has been audited by McGladrey & Pullen, LLP, an independent registered public accounting firm, as stated in their report which is included in this Form 10-K.

### **Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

### **New York Stock Exchange Certification**

Pursuant to Section 303A.12(a) of the New York Stock Exchange Listed Company Manual, the Company submitted an unqualified certification of our Chief Executive Officer to the New York Stock Exchange on May 15, 2007. The Company has also filed, as exhibits to this Annual Report on Form 10-K, the Chief Executive Officer and Chief Financial Officer Certifications required under the Sarbanes-Oxley Act of 2002.

### **ITEM 9B—OTHER INFORMATION**

None.



## **PART III**

### **ITEM 10—DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information concerning the Company's directors, including the Company's separately designated standing audit committee, and on the Company's code of business conduct and ethics required by this Item is incorporated by reference from the Company's Proxy Statement relating to the 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

Information concerning the Company's executive officers required by this Item is set forth in Item 1 of this Annual Report on Form 10-K under the caption "Executive Officers of the Company."

Information concerning beneficial ownership reporting compliance required by this Item is incorporated by reference from the Company's Proxy Statement relating to 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

### **ITEM 11—EXECUTIVE COMPENSATION**

Information concerning director and executive compensation required by this Item is incorporated by reference from the Company's Proxy Statement relating to the 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

### **ITEM 12—SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information concerning the security ownership of certain beneficial owners and management and related stockholder matters required by this Item is incorporated by reference from the Company's Proxy Statement relating to 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

### **ITEM 13—CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

Information concerning certain relationships and related transactions required by this Item is incorporated by reference from the Company's Proxy Statement relating to the 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

### **ITEM 14—PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information concerning the Company's principal accountant fees and services and the pre-approval policies and procedures of the audit committee of the board of directors required by this Item is incorporated by reference from the Company's Proxy Statement relating to 2008 Annual Meeting of Stockholders scheduled to be held April 23, 2008.

## **PART IV**

### **ITEM 15—EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a) Exhibits and Financial Statement Schedules

(1) Financial Statements can be found under Item 8 of Part II of this Form 10-K

(2) Schedules can be found on Page 84 of this Form 10-K

(3) Listing of Exhibits:

- |              |   |
|--------------|---|
| Exhibit 3.1  | Certificate of Incorporation of the Company, as amended (Incorporated by reference to Exhibits 4.1 and 4.2 to the Form S-3 Registration Statement previously filed by the Company File No. 33-62702).   |
| Exhibit 3.2  | Bylaws of the Company, as amended.  |
| Exhibit 10.1 | Sturm, Ruger & Company, Inc. 1986 Stock Bonus Plan (Incorporated by reference to Exhibit 10.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 1988, as amended by Form 8 filed March 27, 1990, SEC File No. 1-10435).                                   |
| Exhibit 10.2 | Amendment to Sturm, Ruger & Company, Inc. 1986 Stock Bonus Plan (Incorporated by reference to Exhibit 10.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435).   |
| Exhibit 10.3 | Sturm, Ruger & Company, Inc. Supplemental Executive Profit Sharing Retirement Plan (Incorporated by reference to Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435).  |
| Exhibit 10.4 | Agreement and Assignment of Lease dated September 30, 1987 by and between Emerson Electric Co. and Sturm, Ruger & Company, Inc. (Incorporated by reference to Exhibit 10.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435). |
| Exhibit 10.5 | Sturm, Ruger & Company, Inc. Supplemental Executive Retirement Plan (Incorporated by reference to Exhibit 10.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 1995, SEC File No. 1-10435).   |
| Exhibit 10.6 | [Intentionally omitted.]  |

- Exhibit 10.7 Sturm, Ruger & Company, Inc. 1998 Stock Incentive Plan. (Incorporated by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K for the year ended December 31, 1998, SEC File No. 1-10435).
- Exhibit 10.8 Sturm, Ruger & Company, Inc. 2001 Stock Option Plan for Non-Employee Directors (Incorporated by reference to Exhibit 4 to the Form S-8 Registration Statement filed by the Company File No. 33-53234).
- Exhibit 10.9 Agreement and Release, dated as of February 28, 2006, by and between Sturm, Ruger & Company, Inc. and William B. Ruger (Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on April 4, 2006, SEC File No. 1-10435)
- Exhibit 10.10 Sale and Purchase Agreement, dated as of September 26, 2006, by and between Sturm, Ruger & Company, Inc. and Ruger Business Holdings, L.P. (Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on September 26, 2006, SEC File No. 1-10435)
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- Exhibit 10.16 Severance Agreement, dated as of December 15, 2006, by and between Sturm, Ruger & Company, Inc. and Christopher John Killoy (Incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the SEC on December 19, 2006, SEC File No. 1-10435)
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- Exhibit 10.18 Retention and Consultation Agreement, dated December 4, 2007, by and between Sturm, Ruger & Company, Inc. and Robert R. Stutler
- Exhibit 23.1 Consent of McGladrey & Pullen, LLP
- Exhibit 31.1 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Exchange Act.
- Exhibit 31.2 Certification of Treasurer and Chief Financial Officer Pursuant to Rule 13a-14(a) of the Exchange Act.
- Exhibit 32.1 Certification of the Chief Executive Officer Pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- Exhibit 32.2 Certification of the Treasurer and Chief Financial Officer Pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- Exhibit 99.1 Item 1 LEGAL PROCEEDINGS from the Quarterly Report on Form 10-Q of the Company for the quarter ended September 30, 1999, SEC File No. 1-10435, incorporated by reference in Item 3 LEGAL PROCEEDINGS.
- Exhibit 99.2 Item 1 LEGAL PROCEEDINGS from the Quarterly Report on Form 10-Q of the Company for the quarters ended March 31, and September 30, 2000, SEC File No. 1-10435, incorporated by reference in Item 3 LEGAL PROCEEDINGS.
- Exhibit 99.3 Item 1 LEGAL PROCEEDINGS from the Quarterly Report on Form 10-Q of the Company for the quarter ended September 30, 2005, SEC File No. 1-10435, incorporated by reference in Item 3 LEGAL PROCEEDINGS.
- Exhibit 99.4 Item 1 LEGAL PROCEEDINGS from the Quarterly Report on Form 10-Q of the Company for the quarter ended June 30, 2007, SEC File No. 1-10435, incorporated by reference in Item 3 LEGAL PROCEEDINGS.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

STURM, RUGER & COMPANY, INC.  
(Registrant)

S/THOMAS A. DINEEN  
Thomas A. Dineen  
Vice President, Treasurer and  
Chief Financial Officer  
(Principal Financial Officer)

February 26, 2008  
Date

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

S/MICHAEL O. FIFER 2/26/08  
Michael O. Fifer  
Chief Executive Officer, Director  
(Principal Executive Officer)

S/STEPHEN L. SANETTI 2/26/08  
Stephen L. Sanetti  
President, Director

S/JOHN M. KINGSLEY, JR. 2/26/08  
John M. Kingsley, Jr.  
Director

S/JAMES E. SERVICE 2/26/08  
James E. Service  
Director

S/JOHN A. CONSENTINO, JR. 2/26/08  
John A. Cosentino, Jr.  
Director

S/C. MICHAEL JACOBI 2/26/08  
C. Michael Jacobi  
Director

S/RONALD C. WHITAKER 2/26/08  
Ronald C. Whitaker  
Director

S/STEPHEN T. MERKEL 2/26/08  
Stephen T. Merkel  
Director

## EXHIBIT INDEX

|              | <u>Page No.</u>   |  |
|--------------|---|--|
| Exhibit 3.1  | Certificate of Incorporation of the Company, as amended (Incorporated by reference to Exhibits 4.1 and 4.2 to the Form S-3 Registration Statement previously filed by the Company File No. 33-62702).   |  |
| Exhibit 3.2  | Bylaws of the Company, as amended.  |  |
| Exhibit 10.1 | Sturm, Ruger & Company, Inc. 1986 Stock Bonus Plan (Incorporated by reference to Exhibit 10.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 1988, as amended by Form 8 filed March 27, 1990, SEC File No. 1-10435).                                   |  |
| Exhibit 10.2 | Amendment to Sturm, Ruger & Company, Inc. 1986 Stock Bonus Plan (Incorporated by reference to Exhibit 10.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435).   |  |
| Exhibit 10.3 | Sturm, Ruger & Company, Inc. Supplemental Executive Profit Sharing Retirement Plan (Incorporated by reference to Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435).  |  |
| Exhibit 10.4 | Agreement and Assignment of Lease dated September 30, 1987 by and between Emerson Electric Co. and Sturm, Ruger & Company, Inc. (Incorporated by reference to Exhibit 10.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 1991, SEC File No. 1-10435). |  |
| Exhibit 10.5 | Sturm, Ruger & Company, Inc. Supplemental Executive Retirement Plan (Incorporated by reference to Exhibit 10.5 to the Company's Annual Report on Form 10-K for the year ended December 31, 1995, SEC File No. 1-10435).   |  |
| Exhibit 10.6 | [Intentionally omitted.]  |  |
| Exhibit 10.7 | Sturm, Ruger & Company, Inc. 1998 Stock Incentive Plan. (Incorporated by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K for the year ended December 31, 1998, SEC File No. 1-10435).   |  |
| Exhibit 10.8 | Sturm, Ruger & Company, Inc. 2001 Stock Option Plan for Non-Employee Directors (Incorporated by reference to Exhibit 4 to the Form S-8 Registration Statement filed by the Company File No. 33-53234).  |  |

EXHIBIT INDEX (continued)

|               | <u>Page No.</u>   |  |
|---------------|---|--|
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YEAR ENDED DECEMBER 31, 2007  
STURM, RUGER & COMPANY, INC.

ITEMS 15(a)(2) AND 15(d)  
FINANCIAL STATEMENT SCHEDULE

Sturm, Ruger & Company, Inc.

Item 15(a)(2) and Item 15(d)--Financial Statement Schedule

Schedule II—Valuation and Qualifying Accounts

*(In Thousands)*

| COL. A                                 | COL. B                         | COL. C  |   | COL. D      | COL. E                   |
|--|--------------------------------|---|---|-------------|--------------------------|
| Description                            | Balance at Beginning of Period | ADDITIONS                                       |   | Deductions  | Balance at End of Period |
|  |                                | (1)<br>Charged (Credited) to Costs and Expenses | (2)<br>Charged to Other Accounts—Describe |             |                          |
| Deductions from asset accounts:        |                                |   |   |             |                          |
| Allowance for doubtful accounts:       |                                |   |   |             |                          |
| Year ended December 31, 2007           | <u>\$155</u>                   |   |   | \$ 28 (a)   | <u>\$127</u>             |
| Year ended December 31, 2006           | <u>\$351</u>                   | \$ (81)   |   | \$ 115 (a)  | <u>\$155</u>             |
| Year ended December 31, 2005           | <u>\$373</u>                   |   |   | \$ 22 (a)   | <u>\$351</u>             |
| Allowance for discounts:               |                                |   |   |             |                          |
| Year ended December 31, 2007           | <u>\$206</u>                   | \$998   |   | \$ 971 (b)  | <u>\$233</u>             |
| Year ended December 31, 2006           | <u>\$346</u>                   | \$2,808   |   | \$2,948 (b) | <u>\$206</u>             |
| Year ended December 31, 2005           | <u>\$555</u>                   | \$3,508   |   | \$3,717 (b) | <u>\$346</u>             |
| Excess and obsolete inventory reserve: |                                |   |   |             |                          |
| Year ended December 31, 2007           | <u>\$(5,516)</u>               | \$755   |   | \$2,128 (c) | <u>\$(4,143)</u>         |
| Year ended December 31, 2006           | <u>\$(3,137)</u>               | \$3,217   |   | \$ 838 (c)  | <u>\$(5,516)</u>         |
| Year ended December 31, 2005           | <u>\$(2,698)</u>               | \$ 461  |   | \$ 22 (c)   | <u>\$(3,137)</u>         |

- (a) Accounts written off or (subsequently recovered)
- (b) Discounts taken
- (c) Inventory written off

**Consent of McGladrey & Pullen, LLP**

We consent to the incorporation by reference in the Registration Statements (Nos. 333-84677 and 333-53234) on Form S-8 of Sturm, Ruger & Company, Inc. (the “Company”) of our reports dated February 22, 2008 relating to our audits of the financial statements and internal control over financial reporting, appearing in the Annual Report on Form 10-K of Sturm, Ruger & Company, Inc. for the year ended December 31, 2007.

McGladrey & Pullen, LLP  
Stamford, Connecticut  
February 22, 2008

## CERTIFICATION

I, Michael O. Fifer, certify that:

1. I have reviewed this annual report on Form 10-K (the “Report”) of Sturm, Ruger & Company, Inc. (the “Registrant”);
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Report;
3. Based on my knowledge, the financial statements, and other financial information included in this Report, fairly present in all material respects, the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Report;
4. The Registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Report based on such evaluation; and
  - d) Disclosed in this Report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s most recent fiscal quarter (the Registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting.

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):
- a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: February 26, 2008

S/MICHAEL O. FIFER

Michael O. Fifer  
Chief Executive Officer

## CERTIFICATION

I, Thomas A. Dineen, certify that:

1. I have reviewed this annual report on Form 10-K (the “Report”) of Sturm, Ruger & Company, Inc. (the “Registrant”);
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Report;
3. Based on my knowledge, the financial statements, and other financial information included in this Report, fairly present in all material respects, the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Report;
4. The Registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Report based on such evaluation; and
  - d) Disclosed in this Report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s most recent fiscal quarter (the Registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting.

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):
- a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: February 26, 2008

S/THOMAS A. DINEEN

Thomas A. Dineen  
Vice President, Treasurer and  
Chief Financial Officer

Certification Pursuant to 18 U.S.C. Section 1350,  
As Adopted Pursuant to  
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 10-K of Sturm, Ruger & Company, Inc. (the "Company") for the period ended December 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael O. Fifer, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respect, the financial condition and results of operations of the Company.

Date: February 26, 2008

S/MICHAEL O. FIFER

Michael O. Fifer  
Chief Executive Officer

A signed original of this statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.



Certification Pursuant to 18 U.S.C. Section 1350,  
As Adopted Pursuant to  
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 10-K of Sturm, Ruger & Company, Inc. (the “Company”) for the period ended December 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Thomas A. Dineen, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respect, the financial condition and results of operations of the Company.

Date: February 26, 2008

S/THOMAS A. DINEEN  
Thomas A. Dineen  
Vice President, Treasurer and  
Chief Financial Officer

A signed original of this statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.