

FRANKLIN ELECTRIC CO INC  
Form 10-K  
March 04, 2009

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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended January 3, 2009

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 0-362

FRANKLIN ELECTRIC CO., INC.  
(Exact name of registrant as specified in its charter)

Indiana  
(State or other jurisdiction of incorporation  
or organization)  
400 East Spring Street  
Bluffton, Indiana  
(Address of principal executive offices)

35-0827455  
(I.R.S. Employer Identification No.)

46714-3798  
(Zip Code)

(260) 824-2900  
(Registrant's telephone number, including area code)

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

Common Stock, \$.10 par value	NASDAQ Global Select Market
Preference Stock Purchase Rights	NASDAQ Global Select Market

(Title of each class) (Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act:  
None  
(Title of each class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  
YES  NO

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. (Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

YES  NO

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant at June 28, 2008 (the last business day of the registrant's most recently completed second quarter) was \$873,901,341. The stock price used in this computation was the last sales price on that date, as reported by NASDAQ Global Select Market. For purposes of this calculation, the registrant has excluded shares held by executive officers and directors of the registrant, including restricted shares and except for shares owned by the executive officers through the registrant's ESOP or 401K Plan. Determination of stock ownership by non-affiliates was made solely for the purpose of responding to this requirement and the registrant is not bound by this determination for any other purpose.

Number of shares of common stock outstanding at February 14, 2009:  
23,018,453 shares

#### DOCUMENTS INCORPORATED BY REFERENCE

A portion of the Proxy Statement for the Annual Meeting of Shareholders to be held on April 24, 2009 (Part III).

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## PART I

### ITEM 1. BUSINESS

Franklin Electric Co., Inc. is an Indiana corporation founded in 1944 and incorporated in 1946 that, together with its subsidiaries, designs, manufactures and distributes groundwater and fuel pumping systems, composed primarily of submersible pumps and motors, electronic controls and related parts and equipment. The Company's business consists of two reporting segments based on the principal end market served: the Water Systems segment and the Fueling Systems segment. The Company includes unallocated corporate expenses in an "Other" segment that together with Water and Fueling represent the Company. Except where the context otherwise requires, "Franklin Electric" or the "Company", shall refer to Franklin Electric Co., Inc. and its consolidated subsidiaries.

The principal raw materials used in the manufacture of the Company's products are coil and bar steel, stainless steel, copper wire, and aluminum ingot. Major components are capacitors, motor protectors, forgings, gray iron castings and bearings. Most of these raw materials are available from multiple sources in the United States and world markets. In the opinion of management, no single supply source is critical to the Company's business. Availability of fuel and energy is adequate to satisfy current and projected overall operations unless interrupted by government direction or allocation.

The Company's products are sold in North America, Europe, the Middle East, South Africa, Australia, Mexico, Brazil, Japan, China, and other world markets. The Company's products are sold by its employee sales force and independent manufacturing representatives.

In North America, the Company is continuing the rationalization of manufacturing capacity between the manufacturing complex in Linares, Mexico and its other North American plants. The current realignment plan includes the phased move of approximately 500,000 man hours of manufacturing activity to Linares, approximately 80 percent of which is from Siloam Springs, Arkansas. The transfer is expected to be largely complete by June 2009.

The market for the Company's products is highly competitive and includes diversified accounts by size and type. The Company's Water Systems and Fueling Systems products and related equipment are sold to specialty Water Systems distributors and some original equipment manufactures ("OEMs"), as well as industrial equipment distributors, fuel service station operators, and major oil and utility companies.

Beginning in 2004, the Company began moving to a North American business model in which it sells Water Systems products primarily directly to wholesale specialty Water Systems distributors. Previously, the Company sold its Water Systems products primarily to pump OEMs (i.e., the Company was primarily a supplier of submersible motors and controls to the OEMs) who then re-sold the Water Systems products, usually combined with pumps and related products, to the wholesale specialty Water Systems distributors. To facilitate this transition, the Company acquired several pump manufacturers in the U.S. and Canada. As of the end of fiscal year 2004, approximately 42 percent of the Company's consolidated sales were attributable to two customers, both of which were pump OEMs. In 2008, no single customer accounted for more than 10 percent of the Company's consolidated sales.

The Company offers normal and customary trade terms to its customers, no significant part of which is of an extended nature. Special inventory requirements are not necessary, and customer merchandise return rights do not extend beyond normal warranty provisions.

The Company employed approximately 3,500 persons at the end of 2008.



## Research and Development

The Company incurred research and development expense as follows:

(In millions)

	2008	2007	2006
Research and development expense	\$ 6.8	\$ 7.3	\$ 8.1

These expenses were for activities related to the development of new products, improvement of existing products and manufacturing methods, and other applied research and development.

The Company owns a number of patents, trademarks and licenses. In aggregate, these patents are of material importance in the operation of the business; however, the Company believes that its operations are not dependent on any single patent or group of patents.

## Backlog

The dollar amount of backlog at the end of 2008 and 2007 by segment was as follows:

(In millions)

	2008	2007
Water Systems	\$ 18.6	\$ 21.3
Fueling Systems	2.6	4.5
	\$ 21.2	\$ 25.8

The backlog is composed of written orders at prices adjustable on a price-at-the-time-of-shipment basis for products, primarily standard catalog items. All backlog orders are expected to be filled in fiscal 2009. The Company's sales in the first quarter are generally less than its sales in other quarters due to generally lower construction activity during that period in the northern hemisphere. Beyond that, there is no seasonal pattern to the backlog and the backlog has not proven to be a significant indicator of future sales.

## Environmental Matters

The Company believes that it is in compliance with all applicable federal, state and local laws concerning the discharge of material into the environment, or otherwise relating to the protection of the environment. The Company has not experienced any material costs in connection with environmental compliance, and does not believe that such compliance will have any material adverse effect upon the financial position, results of operation, cash flows, or competitive position of the Company.

## Available Information

The Company's website address is [www.franklin-electric.com](http://www.franklin-electric.com). The Company makes available free of charge on or through its website: its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports, as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission. Additionally, the Company's website also includes the Company's corporate governance guidelines, its Board committee charters, and the Company's code of business conduct and ethics. Information contained on the Company's website is not part of this annual report on Form 10-K.

Business Segments and Products

Segment and geographic information set forth below under Note 18, "Segment and Geographic Information," to the consolidated financial statements is incorporated herein by reference.

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### Water Systems Segment

Water Systems is a global leader in the production and marketing of groundwater pumping systems and is a technical leader in submersible pumps and motors, drives, electronic controls, and monitoring devices. The Water Systems segment designs, manufactures and sells motors, pumps, electronic controls and related parts and equipment primarily for use in submersible water and other fluid system applications.

Water Systems motors and pumps are used principally in submersible applications for pumping fresh water, wastewater, and other liquids in a variety of residential, agricultural, and industrial applications, off-shore drilling, and mining. Water Systems also manufactures electronic drives and controls for the motors which control functionality and provide protection from various hazards, such as electric surges, over-heating, or dry wells and tanks.

During 2008, the Company added two pump manufacturers in its Water Systems segment. In the first quarter of 2008, the Company completed the acquisition of Industrias Schneider SA. Industrias Schneider is a leading Brazilian producer of pumps for the residential, agricultural, and light commercial markets. The acquisition advances the Company's strategy to expand its business base in developing regions where product demand is growing rapidly. In the second quarter of 2008, the Company acquired Western Pumps LLC, located in Fresno, California. Western Pump designs, develops, and manufactures centrifugal pumps specific to the water truck, agricultural irrigation, and center pivot industries and was targeted to expand growth on the west coast of the United States as well as broaden the Company's product offerings. Industrias Schneider sales were not material as a component of the Company's consolidated sales for 2008. On a pro forma annual basis, Western Pump sales were not material as a component of the Company's consolidated sales for 2008.

In 2008, Water Systems segment research and development expenditures were primarily related to:

- § A new line of 4" pumps with a different construction
- § New additions to sprinkler pump market
- § Addition to the tri-seal line to round out offering
- § New SubDrive that can survive difficult environments
- § New fountain motor aimed at high flow, shallow set applications
- § New condensate pumps for heating, ventilation, and air conditioning (HVAC) applications

### Fueling Systems Segment

Fueling Systems is a global leader in the production and marketing of fuel pumping systems and is a technical leader in electronic controls and monitoring devices. This segment designs, manufactures and sells pumps, electronic controls and related parts and equipment primarily for use in submersible fueling system applications. It also integrates and sells motors and electronic controls produced by the Water Systems segment.

Along with the fueling motor and pump applications, Fueling Systems supplies a variety of products to the petroleum equipment industry included in the submersible pumping systems, such as flexible piping, vapor recovery systems and components, electronic tank monitoring equipment, and fittings. The vapor recovery systems and components have enjoyed particular success in California, due to California Air Resource Board certification.

In 2008, Fueling Systems segment research and development expenditures were primarily related to:

- § DTU Wireless Technology that allows the installation of the Company's Incon ISD vapor monitoring systems quickly, without the need to break concrete to connect to the Company's Healy fuel dispenser mounted sensors
- § A new API bottom loading tank truck valve with enhanced features for the tank truck market
- § A new 15 gallon secondary contained Spill Container, that handles large overfill events at the service station, installation is achieved without the need to break concrete

## ITEM 1A. RISK FACTORS

The following describes the principal risks affecting the Company and its business. Additional risks and uncertainties, not presently known to the Company or currently deemed material, could negatively impact the Company's results of operations or financial condition in the future.

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The Company's acquisition strategy entails expense, integration risks, and other risks.

One of the Company's continuing strategies is to increase revenues and expand market share through acquisitions that will provide complementary Water and Fueling Systems products. The Company spends significant time and effort expanding existing businesses through identifying, pursuing, completing, and integrating acquisitions. Competition for acquisition candidates may limit the number of opportunities and may result in higher acquisition prices. There is uncertainty related to successfully acquiring, integrating and profitably managing additional businesses without substantial costs, delays or other problems. There can also be no assurance that acquired companies will achieve revenues, profitability or cash flows that justify the investment in them. Failure to manage or mitigate these risks could adversely affect the Company's earnings and financial condition.

The Company's products are sold in highly competitive markets, by numerous competitors whose actions could negatively impact sales volume, pricing and profitability.

The Company is a global leader in the production and marketing of groundwater and fuel pumping systems. End user demand, distribution relationships, industry consolidation, new product capabilities of the Company's competitors or new competitors, and many other factors contribute to a highly competitive environment. Additionally, some of the Company's competitors have substantially greater financial resources than the Company. Although the Company believes that consistency of product quality, timeliness of delivery, service, and continued product innovation, as well as price, are principal factors considered by customers in selecting suppliers, competitive factors described above may lead to declines in sales or in the prices of all the Company's products which could have an adverse impact on profitability and financial condition.

The Company's business may be adversely affected by the current economic environment.

The recent worldwide financial and credit market disruptions and uncertainty have reduced the availability of credit generally necessary to fund a continuation and expansion of global economic activity. The shortage of credit combined with recent substantial declines in equity markets and other economic developments could lead to an extended worldwide economic recession. A general slowdown in economic activity caused by a recession could adversely affect our business in several ways. A continuation or worsening of the current difficult financial and economic conditions could reduce sales and adversely affect our customers' ability to meet the terms of sale and our suppliers' ability to fully perform their commitments to us. Given this uncertainty, the Company cannot predict what additional credit may be available in the future. If additional credit is not available, it may have an adverse impact on the Company's ability to complete acquisitions, develop new products or restructure existing operations as well as other negative effects. The cost of new credit in the future may also be higher than the existing credit arrangements the Company currently has in place.

In addition, the financial disruption may have an effect on the Plan assets of the Defined Benefit Plans. The amount of contributions necessary or desirable to be made to the Plan by the Company during the Company's fiscal year 2009 is estimated at \$15.7 million. A continuation of the volatility of interest rates and negative equity returns under current market conditions may result in greater contributions to the Plans in the future.

A decline in housing starts could lead to reduced demand for the Company's products, thereby reducing revenues and earnings.

Demand for certain Company products is affected by housing starts. A decline in housing starts or general slowdown in the United States or other economies in the international markets the Company serves, such as those presently occurring in the United States and many other markets, could reduce demand and adversely impact gross margins and operating results.

Increases in the prices of raw materials, components, finished goods and other commodities could adversely affect operations.

The Company purchases most of the raw materials for its products on the open market and relies on third parties for the sourcing of certain finished goods. Accordingly, the cost of its products may be affected by changes in the market price of raw materials, sourced components, or finished goods. Natural gas and electricity prices have historically been volatile. The Company does not generally engage in commodity hedging for raw materials. Significant increases in the prices of commodities, sourced components, finished goods, or other commodities could cause product prices to increase, which may reduce demand for products or make the Company more susceptible to competition. Furthermore, in the event the Company is unable to pass along increases in operating costs to its customers, margins and profitability may be adversely affected.

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The Company is exposed to political, economic and other risks that arise from operating a multinational business. The Company has significant operations outside the United States, including Europe, South Africa, Brazil, Mexico and China. Further, the Company obtains raw materials and finished goods from foreign suppliers. Accordingly, the Company's business is subject to political, economic, and other risks that are inherent in operating a multinational business. These risks include, but are not limited to, the following:

- Difficulty in enforcing agreements and collecting receivables through foreign legal systems
  - Trade protection measures and import or export licensing requirements
  - Imposition of tariffs, exchange controls or other restrictions
- Difficulty in staffing and managing widespread operations and the application of foreign labor regulations
  - Compliance with foreign laws and regulations
- Changes in general economic and political conditions in countries where the Company operates

Additionally, the Company's operations outside the United States could be negatively impacted by changes in treaties, agreements, policies and laws implemented by the United States.

If the Company does not anticipate and effectively manage these risks, these factors may have a material adverse impact on its international operations or on the business as a whole.

Transferring operations of the Company to low cost regions may not result in the intended cost benefits. The Company is continuing its rationalization of manufacturing capacity between all existing manufacturing facilities and the manufacturing complexes in low cost regions such as Mexico, the Czech Republic and China. To implement this strategy, the Company must complete the transfer of assets and intellectual property between operations. Each of these transfers involves the risk of disruption to our manufacturing capability, supply chain and, ultimately, to our ability to service customers and generate revenues and profits.

The Company has significant investments in foreign entities and has significant sales and purchases in foreign denominated currencies creating exposure to foreign currency exchange rate fluctuations. The Company has significant investments outside the United States, including Europe, South Africa, Brazil, Mexico and China. Further, the Company has sales and makes purchases of raw materials and finished goods in foreign denominated currencies. Accordingly, the Company has exposure to fluctuations in foreign currency exchange rates relative to the US dollar. Foreign currency exchange rate risk is reduced through several means: maintenance of local production facilities in the markets served, invoicing of customers in the same currency as the source of the products, prompt settlement of inter-company balances utilizing a global netting system and limited use of foreign currency denominated debt. To the extent that these mitigating strategies are not successful, foreign currency rate fluctuations can have a material adverse impact on its international operations or on the business as a whole.

Delays in introducing new products or the inability to achieve or maintain market acceptance with existing or new products may cause the Company's revenues to decrease. The industries to which the Company belongs are characterized by intense competition, changes in end-user requirements, and evolving product offerings and introductions. The Company believes future success will depend, in part, on the ability to anticipate and adapt to these factors and offer, on a timely basis, products that meet customer demands. Failure to develop new and innovative products or to enhance existing products could result in the loss of existing customers to competitors or the inability to attract new business, either of which may adversely affect the Company's revenues.



Certain Company products are subject to regulation and government performance requirements in addition to the warranties provided by the Company.

The Company's product lines have expanded significantly and certain products are subject to government regulations and standards for manufacture, assembly, and performance in addition to the warranties provided by the Company. The Company's failure to meet all such standards or perform in accordance with warranties could result in significant warranty or repair costs, lost sales and profits, damage to the Company's reputation, and fines or penalties from Governmental organizations. Changes to these standards may require the Company to modify its business objectives and incur additional costs to comply.

The growth of municipal water systems and increased government restrictions on groundwater pumping could reduce demand for private water wells and the Company's products, thereby reducing revenues and earnings.

Demand for certain Company products is affected by rural communities shifting from private and individual water well systems to city or municipal water systems. Many economic and other factors outside the Company's control, including Federal and State regulations on water quality, tax credits and incentives, could impact the demand for private and individual water wells. A decline in private and individual water well systems in the United States or other economies in the international markets the Company serves could reduce demand for the Company's products and adversely impact sales, gross margins and operating results.

Demand for Fueling Systems products is impacted by environmental legislation which may cause significant increases in product demand and may be followed by significantly reduced demand after meeting compliance requirements. Environmental legislation related to air quality and fueling containment may create demand for certain Fueling Systems products which must be supplied in a relatively short time frame to meet the governmental mandate, as is currently occurring in California with respect to vapor control and monitoring systems. During this period of increased demand the Company's revenues and profitability could increase significantly. The Company is at risk of not having capacity to meet demand or cost overruns due to inefficiencies during ramp up to the higher production levels. After the Company's customers have met the compliance requirements, the Company's revenues and profitability may decrease significantly as the demand for certain products declines substantially. The Company is at risk of not reducing production costs in relation to the decreased demand as well as reduced revenues adversely impacting gross margins and operating results.

#### Additional Risks to the Company

The Company is subject to various risks in the normal course of business. Exhibit 99.1 sets forth risks and other factors that may affect future results, including those identified above, and is incorporated herein by reference.

#### ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

#### ITEM 2. PROPERTIES

The Company maintains its principal executive offices in Bluffton, Indiana.

Manufacturing plants or primary distribution centers in the Water Systems segment are located in the following countries: Australia, Brazil, Canada, China, The Czech Republic, Germany, Italy, Japan, Mexico, Republic of Botswana, South Africa, and the United States. Within the United States, significant manufacturing facilities are located in Grant County, Indiana; Little Rock, Arkansas; Siloam Springs, Arkansas; Wilburton, Oklahoma; and

Oklahoma City, Oklahoma.

Manufacturing plants or primary distribution centers in the Fueling Systems segment are located in the following countries: China, Germany, South Africa, and the United States. Within the United States, a significant manufacturing facility is located in Madison, Wisconsin.

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The Company also maintains warehouse facilities in Bluffton, Indiana; Orange, California; Sanford, Florida; Winnipeg, Manitoba, Canada; and Bolton, Ontario, Canada.

In the Company's opinion, its facilities are suitable for their intended use, adequate for the Company's business needs, and in good condition.

### ITEM 3. LEGAL PROCEEDINGS

During the first half of 2008, the Company completed a retrofit program in which it replaced a third party supplied component part in the nozzle of the Enhanced Vapor Recovery Systems installed in California filling stations. In October 2008, the California Air Resources Board ("CARB") provided a Notice of Violation to the Company alleging that the circumstances leading to the retrofit program violated California statutes and regulations. Proceedings under the NOV are not expected to adversely affect the Company's sale of Enhanced Vapor Recovery Systems in California. The Company intends to attempt to resolve this matter in discussions with CARB, as CARB invited it to do, and does not expect the resolution of this matter, and any related proceedings involving local agencies, to have a material effect on the Company's financial position, results of operations, and cash flows.

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## EXECUTIVE OFFICERS OF THE REGISTRANT

Current executive officers of the Company, their ages, current position, and their business experience during at least the past five years as of January 3, 2009 are as follows:

Name	Age	Position Held	Period Holding Position
R. Scott Trumbull	60	Chairman of the Board and Chief Executive Officer	2003-present
Peter C. Maske	58	Senior Vice President and President of Europa	1999-present
Gregg C. Sengstack	50	Senior Vice President and President International & Fueling Group	2005-present
		Senior Vice President, Chief Financial Officer	2001-2005
Robert J. Stone	44	Senior Vice President and President Americas Water Systems	2007-present
		Vice President of Sales, Marketing, and Engineering of Western Hemisphere Water Systems	2004-2007
Thomas J. Strupp	55	Vice President, Franklin Electric and President of the Water Transfer Systems	2008-present
		Vice President, Chief Financial Officer, Secretary, and President Water Transfer Systems	2005-2008
		Vice President of Sales and Marketing, Pentair Water Group, Inc., a company specializing in water flow and filtration systems, and enclosures that house electrical components	2004-2005
Daniel J. Crose	60	Vice President and Director of North American Operations	2003-present
Gary D. Ward	53	Vice President and Director of Human Resources	2004-present
Delancey W. Davis	43	Vice President and Business Unit Manager US/Canada Water Systems	2008-present
		Vice President and Director of Sales Western Hemisphere Water Systems	2005-2008
		Vice President of Sales and Marketing, Flexcon Industries, a company specializing in the manufacture of pressurized diaphragm expansion tanks for water wells	1999-2005
John J. Haines	45	Vice President, Chief Financial Officer and Secretary	2008-present
		Managing Director and Chief Executive Officer, HSBC Auto Finance, a provider of consumer automobile financing	2004-2008

All executive officers are elected annually by the Board of Directors at the Board meeting held in conjunction with the annual meeting of shareowners. All executive officers hold office until their successors are duly elected or until their death, resignation, or removal by the Board.



## PART II

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

The number of shareowners of record as of February 14, 2009 was 994. The Company's stock is traded on NASDAQ Global Select Market: Symbol FELE.

Dividends paid and the price range per common share as quoted by the NASDAQ Global Select Market for 2008 and 2007 were as follows:

	DIVIDENDS PER SHARE		PRICE PER SHARE			
	2008	2007	2008		2007	
			Low	High	Low	High
1st Quarter	\$ .120	\$ .110	\$ 30.71	\$ 40.49	\$ 44.68	\$ 52.08
2nd Quarter	\$ .125	\$ .120	\$ 32.77	\$ 44.99	\$ 41.87	\$ 49.90
3rd Quarter	\$ .125	\$ .120	\$ 35.02	\$ 54.55	\$ 40.00	\$ 52.55
4th Quarter	\$ .125	\$ .120	\$ 23.76	\$ 44.00	\$ 36.07	\$ 47.60

Issuer Purchases of Equity Securities:

The Company did not purchase, under the Company's stock repurchase program, any shares of its common stock during the three months ended January 3, 2009.

## ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with the Company's consolidated financial statements. The information set forth below is not necessarily indicative of future operations.

## FIVE YEAR FINANCIAL SUMMARY (a)

	2008	2007	2006	2005	2004
	(b)	(c)	(d)	(e)	(f)
Operations:					
Net sales	\$ 745,627	\$ 602,025	\$ 557,948	\$ 403,413	\$ 370,070
Gross profit	226,925	172,820	191,557	142,821	126,191
Interest expense	10,968	8,147	3,373	766	488
Income tax expense	22,925	15,434	30,671	24,953	21,126
Income from continuing operations	44,111	28,683	56,762	45,796	38,368
Depreciation and amortization	24,164	20,359	17,989	14,971	15,143
Capital expenditures	25,641	28,281	23,190	17,845	21,110
Balance sheet:					
Working capital (g)	\$ 236,248	\$ 218,830	\$ 123,833	\$ 138,998	\$ 111,697
Property, plant and equipment, net	144,535	134,931	115,976	95,732	95,924
Total assets	694,057	662,237	526,925	379,762	333,473
Long-term debt	185,528	151,287	51,043	12,324	13,752
Shareowners' equity	348,937	378,544	345,831	267,562	234,333
Other data:					
Income from continuing operations, to sales	5.9%	4.8%	10.2%	11.4%	10.4%
Income from continuing operations, to average total assets	6.5%	4.8%	12.5%	12.8%	12.5%
Current ratio (h)	3.9	3.4	2.3	3.2	3.1
Number of common shares outstanding	23,018	23,091	23,009	22,485	22,041
Per share:					
Market price range					
High	\$ 54.55	\$ 52.55	\$ 62.95	\$ 45.29	\$ 43.48
Low	23.76	36.07	38.70	34.54	29.01
Income, from continuing operations, per weighted-average common share	1.92	1.24	2.49	2.06	1.75
Income, from continuing operations, per weighted-average common share, assuming dilution	1.90	1.22	2.43	1.97	1.67
Book value (i)	15.02	16.12	14.84	11.54	10.17
Dividends per common share	0.50	0.47	0.43	0.38	0.31

(a) The five year financial presentation excludes the sales and earnings of the Engineered Motor Products Division (EMPD) which was sold during the fourth quarter of 2006, for 2004 to 2006.

(b) Includes the results of operations of the Company's wholly-owned subsidiaries, Industrias Schneider SA, and Western Pump, since their acquisitions in the first and second quarter of 2008, respectively.

(c) Includes the results of operations of the Company's wholly-owned subsidiaries, Pump Brands and the pump division of Monarch, since their acquisitions in the second and third quarters of 2007, respectively.

(d) Includes the results of operations of the Company's wholly-owned subsidiaries, Little Giant Pump Company and Healy Systems, Inc., since their acquisition in the second and third quarters of 2006, respectively.

(e) Includes the results of operations of the Company's wholly-owned subsidiary, Phil-Tite Enterprises, and the effect of an equity investment in Pioneer Pump, Inc., both acquired in the third quarter of 2005.

(f) Includes the results of operations of the Company's wholly-owned subsidiary, Franklin Pump Systems, since the acquisition of certain assets of JBD, Inc. in the third quarter of 2004.

(g) Working capital = Current assets minus Current liabilities.

(h) Current ratio = Current assets divided by Current liabilities.

(i) Book value = Shareowners equity divided by weighted average common shares, assuming full dilution.

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

2008 // 2007

## OVERVIEW

Sales for 2008 were up a total of 24 percent from 2007. About 15 percent is attributable to sales from the Company's acquisitions and about 9 percent from organic growth. Fueling Systems product sales increased to 25 percent of the Company's total 2008 sales from about 22 percent in 2007. Earnings increased in 2008 primarily due to the higher sales volume and product mix changes. Fueling Systems product sales increased about 40 percent from 2007 resulting in significant earnings improvement as the Segment leveraged its fixed costs. Sales growth of the Company slowed significantly in the fourth quarter of 2008 primarily as a result of broad economic deterioration in our end markets.

## RESULTS OF OPERATIONS

## Net Sales

	2008	2007	2008 v 2007
	Net Sales		
Water Systems	\$ 557.0	\$ 466.8	\$ 90.2
Fueling Systems	\$ 188.6	\$ 135.2	\$ 53.4
Other	\$ -	\$ -	\$ -
Consolidated	\$ 745.6	\$ 602.0	\$ 143.6

Net sales for 2008 were \$745.6 million, an increase of \$143.6 million or about 24 percent compared to 2007 sales of \$602.0 million. The full year incremental impact of sales from businesses acquired during 2007 and acquisitions in 2008 was \$87.7 million. Sales revenue increased by \$6.3 million or about 1 percent in 2008 due to foreign exchange rate changes. However the U.S. dollar strengthened against most foreign currencies late in 2008, negatively impacting fourth quarter sales. Overall organic growth for 2008, including foreign exchange rate changes, was \$55.9 million or about 9 percent.

## Net Sales-Water Systems

Globally, Water Systems sales increased in 2008 by about 19 percent from 2007. The increase in Water Systems sales was due primarily to sales attributable to acquisitions. Excluding acquisitions, Water Systems sales increased by about 1 percent versus 2007. Sales growth was impacted by the reduction in the number of new housing starts in the United States and portions of Western Europe and a reduction in inventory held by distributors and contractors. Management expects the reduction in new housing starts and inventory to continue into 2009.

## Net Sales-Fueling Systems

Globally, Fueling Systems sales for 2008 were \$188.6 million, an increase of \$53.4 million or about 40 percent compared to 2007. All of the sales increase was organic. Fueling revenue growth was led by vapor recovery system sales in California. Management estimates that as of year end 2008, 45 to 50 percent of the 11,200 filling stations in California have installed vapor control systems and that Franklin Fueling Systems has supplied over 90 percent of these installations. In late 2008, the rate of vapor recovery system installations in California slowed. The Company believes that some of this slowing is due to the general economic environment and the difficulty station owners are having in obtaining debt financing for new equipment. Additionally, a competitive vapor management control system was introduced by Veeder Root. The Company filed a lawsuit (i) alleging that Veeder Root, in an effort to gain

market share, has engaged in unfair competition and (ii) seeking to prevent any further adverse effect on the Company's business in California. The Company expects that it will continue to win a majority share of the remaining California installations.

Fueling Systems sales also increased in key international markets including China, other areas of Asia, and Latin America during the year.

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#### Cost of Sales

Cost of sales as a percent of net sales for 2008 and 2007 was 69.6 percent and 71.3 percent, respectively. Correspondingly, the gross profit margin increased to 30.4 percent from 28.7 percent. The Company's gross profit was \$226.9 million, up by \$54.1 million from the \$172.8 million in 2007. Of the \$54.1 million increase, about \$29.0 was the result of volume and sales mix improvements; and about \$26.9 million was attributable to acquisitions. Gross profit was reduced by \$6.8 million as a result of reduced facility utilization consistent with management's plan to reduce finished goods inventory and increase inventory turns over the course of the year. Sales price was also a factor in the gross profit increase, partially offset by higher material, freight and warranty expenses in the year versus 2007. During the fourth quarter of 2008 raw materials commodity costs declined significantly. Management believes commodity costs will be lower on average in 2009 than in 2008.

#### Selling, General and Administrative ("SG&A")

Selling and administrative ("SG&A") expense as a percent of net sales for 2008 and 2007 was 19.8 percent and 19.9 percent, respectively. SG&A expense spending increased by \$28.2 million in 2008 compared to last year. The acquisitions of Pump Brands (South Africa), the pump division of Monarch Industries (Canada), Industrias Schneider SA (Brazil), Western Pumps and Cal Pump (United States) added approximately \$18.0 million of selling, general and administrative expenses to the Water Systems segment during 2008. Excluding acquisitions, the Company's overall marketing and selling expenses in 2008 increased by \$3.7 million to prior year. Additionally, expenses related to variable performance based compensation increased by approximately \$3.9 million in 2008 versus 2007.

#### Restructuring Expenses

There were \$2.2 million of nonrecurring restructuring expenses in 2008 compared to \$3.9 million in 2007. In December 2008, the Company announced Phase 3 of its Global Manufacturing Realignment Program for its manufacturing facilities in North America and Brazil. In North America the Company is continuing the rationalization of manufacturing capacity between the manufacturing complex in Linares, Mexico and its other North American plants. Initially, Phase 3 of the realignment plan includes the phased move of approximately 500,000 man hours of manufacturing activity to Linares, approximately 80 percent of which is from Siloam Springs, Arkansas. The transfer is expected to be largely complete by June, 2009 and is anticipated to reduce manufacturing labor and overhead costs. The Company has estimated the pretax charge at \$6.0 million to \$8.0 million over three to four quarters beginning with the fourth quarter of 2008 and includes severance expenses, pension charges, asset write-offs, and equipment relocation costs. Approximately two thirds of these charges will be non-cash. After this transfer is complete, the Linares facility will have sufficient capacity to absorb additional manufacturing activity and plans are being made to further rationalize capacity in late 2009 and 2010.

In Brazil, in order to support sales growth, the Company will transfer its manufacturing operations in Joinville to a new facility and will sell the existing facility. The Company believes this transfer will begin in late 2009 or early 2010. It is anticipated that relocation costs for this move will be approximately \$0.3 million. When more definitive estimates of the timing and costs of the transfer are known, the Company will announce them.

During the first quarter of 2007, the Company initiated Phase 2 of its Global Manufacturing Realignment Program. Phase 2 of the realignment plan included expanding facilities in low-cost regions and shifting production out of higher cost manufacturing facilities. During the first quarter 2008, having finished construction of the new pump plant in Linares, Mexico and the consolidation of other manufacturing facilities, the Company completed Phase 2 of the Global Manufacturing Realignment Program. In total, this phase included severance and equipment relocation costs of \$4.0 million pre-tax, with \$3.9 million in 2007 and \$0.1 million in the first quarter 2008. As previously disclosed, Phase 1 of the realignment plan, which was completed in December 2005, resulted in \$7.5 million of pre-tax restructuring expenses

### Operating Income

Operating income was \$76.7 million in 2008, up \$27.5 million from 2007 operating income of \$49.2 million.

	2008	2007	2008 v 2007
	Operating income/ (loss)		
Water Systems	\$ 67.6	\$ 56.7	\$ 10.9
Fueling Systems	\$ 49.4	\$ 24.6	\$ 24.8
Other	\$ (40.3)	\$ (32.1)	\$ (8.2)
Consolidated	\$ 76.7	\$ 49.2	\$ 27.5

### Operating Income-Water Systems

Water Systems operating income was \$67.6 million for 2008, up \$10.9 million or about 19 percent versus the same period a year ago. Operating margins were basically unchanged at 12.1 percent to sales in 2008 versus in the prior year of 12.2 percent.

### Operating Income-Fueling Systems

Fueling Systems operating income was \$49.4 million, an increase of \$24.8 million or about 100 percent versus 2007. Operating margins improved to 26.2 percent of sales versus 18.2 percent in the prior year percent. Fueling Systems operating income improved primarily as a result of sales volume increases.

### Operating Income-Other

Operating income other is composed primarily of unallocated general and administrative expenses. General and administrative expense increases were primarily due to higher compensation expenses. Other SG&A increases were related to the realignment of general and administrative expenses of acquired companies within the Water Systems segment into the corporate structure.

### Interest Expense

Interest expense for 2008 and 2007 was \$11.0 million and \$8.1 million, respectively. Interest expense increased in 2008 due primarily to debt increases associated with the acquisitions, as well as increased working capital.

### Other Income or Expense

Other Income or Expense for 2008 and 2007 was \$1.3 million income and \$3.0 million income, respectively. Included in "Other income" for both 2008 and 2007 was interest income of \$2.1 and \$2.2 million, primarily derived from the investment of cash balances in short-term U.S. treasury and agency securities. Also, included in other income in 2008 and 2007 was income from equity investments of \$0.7 million and \$0.9 million. In 2008, the Company reached an agreement in principle to settle a trademark licensing dispute and recorded a pre-tax expense of \$0.9 million to reflect the settlement payment.

### Foreign Exchange

For 2008 foreign currency-based transactions were not significant and were a gain of about \$0.1 million for 2007.

### Income Taxes

The provision for income taxes in 2008 and 2007 was \$22.9 million and \$15.4 million, respectively. The effective tax rates for 2008 and 2007 were 34.2 and 35.0 percent, respectively. The effective tax rate differs from the United States statutory rate of 35 percent, generally due to foreign income exclusion and due to the effects of state and foreign income taxes, net of federal tax benefits.

### Net Income

Net income for 2008 was \$44.1 million, or \$1.90 per diluted share, compared to the same period of 2007 net income of \$28.7 million or \$1.22 per diluted share.

2007 // 2006

## OVERVIEW

Sales for 2007 were up from 2006. The increase in sales was primarily related to sales from acquisitions. Sales growth was further benefited by significant organic growth in Water Systems pump unit shipments and international sales of Water Systems products, as well as organic growth in Fueling Systems product shipments, primarily vapor recovery systems. Earnings declined in 2007 primarily due to the decreased sales of submersible motor units in the United States and Canada. The Company's margins were also impacted by higher commodity costs, increased fixed costs incurred in connection with manufacturing, engineering, selling, general and administrative spending resulting from the Company's strategy of selling to a more diversified customer base by marketing its Water Systems products direct to distributors as well as price discounting in the submersible motor and pump industry within the United States and Canada. The Company also incurred significant restructuring costs related to the 2007 phase of its Global Manufacturing Realignment program, which also decreased operating income.

## RESULTS OF OPERATIONS

## Net Sales

(In millions)	2007	2006	2007 v 2006
	Net sales to external customers		
Water Systems	\$ 466.8	\$ 465.6	\$ 1.2
Fueling Systems	\$ 135.2	\$ 92.3	\$ 42.9
Other	-	-	-
Consolidated	\$ 602.0	\$ 557.9	\$ 44.1

Net sales for fiscal year 2007 were \$602.0 million, an increase of \$44.1 million or 8 percent compared to 2006 sales of \$557.9 million. Excluding acquisition related sales and changes in foreign exchange rates; net sales decreased about 8 percent. Incremental sales related to acquisitions for fiscal year 2007 were about \$79 million or 14 percent of prior year sales. Acquisition sales growth was attributable to the full year impact on 2007 of the Little Giant Pump Company and Healy Systems acquisitions from 2006, as well as the 2007 acquisitions of Pump Brands and the pump division of Monarch. The Company also realized organic growth in Fueling Systems sales and in all submersible Water Systems sales in regions outside the United States and Canada.

## Net Sales-Water Systems

Water Systems sales worldwide were \$466.8 million, up \$1.2 million for fiscal year 2007 compared to 2006. Excluding acquisition related sales and changes in foreign exchange rates; net sales decreased about 15 percent. The decrease was primarily attributable to a significant decline in unit sales of 4 inch submersible motors in the United States and Canada. Partially offsetting the decline was a significant increase in pump product unit sales in the United States and Canada, as well as increases across all submersible product sales outside of the region.

## Net Sales-Fueling Systems

Fueling Systems sales worldwide were \$135.2 million an increase of approximately 47 percent in 2007 from fiscal year 2006. Fueling Systems sales growth benefited from both organic sales growth, primarily related to vapor recovery systems and electronic fuel management systems, as well as acquisition related sales. Excluding acquisition related sales and changes in foreign exchange rates; net sales increased about 29 percent.

## Cost of Sales

Cost of sales as a percent of net sales for 2007 and 2006 was 71.3 percent and 65.7 percent, respectively. Cost of sales as a percent of net sales increased in 2007 from 2006 primarily as a result of product mix changes as Fueling Systems products and complete Water Systems pumps (including Little Giant product lines) represented a higher percentage of overall sales and these product lines carry a higher cost of sales than submersible motor products. Fixed costs increased as a percentage of sales for Water Systems sales in the United States as shipments declined faster than related costs. Other less significant increases in cost of sales during 2007 were freight, warranty and obsolescence expenses.

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### Restructuring expenses

During 2007, the Company continued to execute its Global Manufacturing Realignment program. This phase included the expansion of small submersible motor manufacturing in Linares, Mexico; the construction and start-up of a new pump manufacturing plant in Linares; the consolidation of Fueling Systems operations into the recently enlarged Madison, Wisconsin plant; and the streamlining of motor manufacturing operations in Siloam Springs, Arkansas and Wittlich, Germany. The Company also announced the phased relocation of the Little Rock, Arkansas Water Systems pump manufacturing to the new pump plant in Linares, Mexico. Restructuring expenses for 2007 were approximately \$3.9 million (pre-tax) and reduced diluted earnings per share by approximately \$0.11 per share for year ending December 2007. Full year 2007 restructuring expenses include severance and other employee expenses as well as manufacturing equipment relocation costs.

### Selling, General and Administrative (“SG&A”)

SG&A expense as a percent of net sales for 2007 and 2006 was 19.9 percent and 18.4 percent, respectively. The increase in SG&A was about \$17.3 million in 2007 over 2006, \$13.2 million of which was due to acquisitions. Other increases in SG&A costs were incurred in connection with selling, general and administrative spending resulting from the Company’s strategy of selling to a more diversified customer base by marketing its Water Systems products directly to distributors and increased variable commissions on stronger Fueling Systems sales.

### Operating Income

(In millions)	2007	2006	2007 v 2006
	Operating income/ (loss)		
Water Systems	\$ 56.7	\$ 104.4	\$ (47.7)
Fueling Systems	\$ 24.6	\$ 15.0	\$ 9.6
Other	\$ (32.1)	\$ (30.3)	\$ (1.8)
Consolidated	\$ 49.2	\$ 89.1	\$ (39.9)

### Operating Income-Water Systems

Water Systems operating income decreased primarily as a result of lower unit sales of 4” submersible motors to major OEMs in the US and Canada. In addition, other factors affecting the decrease in operating income for the Water Systems segments were product mix changes, about \$5.5 million primarily from declining motor shipments as a percentage of Water Systems sales, higher freight costs of \$4.5 million, slow moving and obsolescence expense of \$1.4 million related to change over and implementing new product designs, and warranty costs of \$0.8 million. Partially offsetting the decline in operating income were earnings from acquisitions and increased Water Systems product sales and related earnings from regions outside of the US and Canada.

### Operating Income-Fueling Systems

Fueling Systems operating income improved primarily as a result of sales volume increases. Fueling Systems margins improved by 90 basis points due to the product mix benefit of the sales growth and as sales increased at a greater rate than fixed manufacturing costs.

### Operating Income-Other

Other operating income is composed primarily of unallocated general and administrative expenses. General and administrative expense increases were primarily due to increased expenses associated with acquisitions.

### Interest expense

Interest expense for 2007 and 2006 was \$8.1 million and \$3.4 million, respectively. Interest expense increased in 2007 due to the debt incurred for acquisitions and increased working capital requirements.

### Other income or expense

Included in other income for 2007 and 2006 was interest income of \$2.2 million and \$1.9 million, respectively, primarily derived from the investment of cash balances in short-term U.S. treasury and agency securities. Also,

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included in other income for 2007 and 2006 was income from equity investments of \$0.9 million and \$0.7 million, respectively.

#### Foreign exchange

Foreign currency-based transactions produced a gain for 2007 of about \$0.1 million primarily due to rate changes of the euro, the Canadian dollar and the South African Rand relative to the U.S. dollar. Foreign currency-based transactions produced a loss for 2006 of \$0.1 million primarily due to euro rate changes relative to other currencies in Europe and the U.S. dollar.

#### Income taxes

The provision for income taxes from continuing operations in 2007 and 2006 was \$15.4 million and \$30.7 million, respectively. The effective tax rates were 35.0 and 35.1 percent for 2007 and 2006, respectively. The effective tax rate differs from the United States statutory rate of 35 percent, generally due to foreign income exclusion and R&D credits and due to the effects of state and foreign income taxes, net of federal tax benefits.

#### Income from continuing operations

Income from continuing operations for 2007 was \$28.7 million, or \$1.22 per diluted share, compared to 2006 income from continuing operations of \$56.8 million or \$2.43 per diluted share.

### CAPITAL RESOURCES AND LIQUIDITY

The Company's primary sources of liquidity are cash flows from operations and funds available under its committed, unsecured, revolving credit agreement maturing 2011 (the "Agreement") in the amount of \$120.0 million and its amended and restated uncommitted note purchase and private shelf agreement (the "Prudential Agreement") in the amount of \$175.0 million. The Company has no scheduled principal payments on the Prudential Agreement until 2015. As of January 3, 2009 the Company had \$85.0 million and \$25.0 million of borrowing capacity under the respective agreements. The uncertainty in the financial and credit markets has not impacted the liquidity of the Company and the Company expects that ongoing requirements for operations, capital expenditures, dividends, and debt service will be adequately funded from its existing credit agreements. The Agreement and the Prudential Agreement do not contain any material adverse changes or similar provisions that would accelerate the maturity of amounts drawn under either agreement. The Agreement and Prudential Agreement do contain various customary conditions and covenants, which limit, among other things, borrowings, interest coverage, loans or advances and investments. As of January 3, 2009, the Company was in compliance with all covenants.

Net cash flows from operating activities were \$44.4 million in 2008 compared to \$4.2 million in 2007 and \$55.4 million in 2006. The operating cash flow improvement was largely a result of greater Fueling Systems income from continuing operations and normal fluctuations in operating assets and liabilities related to overall results of operations. Fueling revenue growth was led by strong vapor recovery system sales in California.

Net cash used in investing activities was \$65.0 million in 2008 compared to \$63.2 million in 2007 and \$131.6 million in 2006. The 2008 activities were primarily related to \$38.4 million, net of cash acquired, used to acquire Industrias Schneider on January 9, 2008. The acquisition was funded with cash and long term borrowings under the Agreement. Additionally, \$25.6 million was used for property, plant and equipment additions in 2008. During 2007 the Company acquired Pump Brands in the second quarter and the pump division of Monarch Industries Limited in the third quarter at an aggregate purchase price of \$37.0 million, net of cash acquired, and utilized \$28.3 million to fund property, plant and equipment additions. In 2006, the Company completed its acquisition of Little Giant Pump Company for a cash purchase price of \$120.8 million and Healy Systems, Inc. in a stock purchase transaction for a cash purchase price of \$35.1 million. Additionally, \$23.1 million was used to fund property, plant and equipment additions in 2006.

Net cash provided by financing activities of \$8.9 million in 2008 was primarily related to proceeds from new debt incurred, net of repayments to date. Also included was the repurchase of approximately 235,000 shares of its common stock for \$7.8 million and the payment of \$11.4 million in dividends to its shareholders. Net cash provided by financing activities of \$87.0 million in 2007 was primarily related to proceeds from new debt incurred, net of repayments to date, the repurchase of approximately 187,600 shares of its common stock for \$8.1 million, and the payment of \$10.8 million in dividends to its shareholders. In 2006, net cash provided by financing activities of

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\$54.8 million was primarily related to proceeds from new debt incurred, net of repayments to date, as well as the payment of \$9.8 million in dividends to its shareholders.

#### 2008 AGGREGATE CONTRACTUAL OBLIGATIONS

Most of the Company's contractual obligations to third parties are debt obligations. In addition, the Company has certain contractual obligations for future lease payments, contingency payments, as well as, purchase obligations. The payment schedule for these contractual obligations is as follows:

(In millions)	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Debt	\$ 185.0	\$ 0.0	\$ 35.0	\$ 0.0	\$ 150.0
Debt interest	76.1	9.5	18.5	17.7	30.4
Capital leases	1.2	0.7	0.4	0.1	0.0
Operating leases	20.4	5.6	7.2	2.4	5.2
Contingencies from acquisitions (Healy Systems and Western Pump)	0.6	0.6	0.0	0.0	0.0
Purchase obligations	2.1	2.1	0.0	0.0	0.0
	\$ 285.4	\$ 18.5	\$ 61.1	\$ 20.2	\$ 185.6

Debt interest includes interest under the Company's current credit agreement. The average interest rate for 2008 was 3.2 percent based on the LIBOR plus an interest spread. The remaining interest calculated was based on the fixed rate of 6.31 percent for the Company's short-term insurance company debt and 5.79 percent for the Company's long-term insurance company debt.

The Healy Systems stock purchase agreement provided for additional contingent payments of 5 percent of certain Healy Systems product sales over the next five years from the year of acquisition. The Western Pump stock purchase agreement provided for additional contingent payments of 7.5 percent of business net sales for the two year period commencing April 1, 2008; however the aggregate amount shall not exceed \$0.8 million.

The Company has pension and other post-retirement benefit obligations not included in the table above which will result in future payments of \$15.7 million. The Company also has unrecognized tax benefits related to FASB Interpretation 48 obligations, none of which are included in the table above. The unrecognized tax benefits of approximately \$6.8 million have been recorded as liabilities in accordance with FASB Interpretation No. 48 Uncertainty in Income Taxes, and we are uncertain as to if or when such amounts may be settled. Related to the unrecognized tax benefits, the Company has also recorded a liability for potential penalties and interest of \$0.4 million.

#### ACCOUNTING PRONOUNCEMENTS

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, Fair Value Measurements. This statement defines fair value in generally accepted accounting principles and expands disclosures about fair value measurements that are required or permitted under other accounting pronouncements. This statement was effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company's adoption of this statement in first quarter 2008 had no impact on its consolidated financial position, results of operations and cash flows. The Company also adopted the deferral provisions of SFAS No. 157-2, which delayed the effective date of SFAS No. 157 for all nonrecurring fair value measurements of non-financial assets and liabilities until fiscal years beginning after November 15, 2008. The Company is in the process of determining the impact of adopting SFAS No.

157, for those non-financial assets and liabilities deferred, on its consolidated financial position, results of operations and cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities. This statement permits entities to choose to measure many financial instruments and certain other items at fair value. This statement was effective as of the beginning of the first fiscal year beginning after November 15,

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2007. Upon the Company's adoption of SFAS No. 159, it did not elect the fair value option for any assets or liabilities. Therefore this statement had no impact on the Company's consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations—a replacement of FASB No. 141. SFAS No. 141(R) establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS No. 141(R) is effective for financial statements issued for fiscal years beginning after December 15, 2008. Earlier adoption is prohibited. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position, results of operations and cash flows. SFAS No. 141(R) generally applies to acquisitions completed after its effective date.

In December 2007, the FASB issued SFAS No. 160, Non-controlling Interests in Consolidated Financial Statements—an amendment of Accounting Research Bulletin (“ARB”) No. 51. SFAS No. 160 (a) amends ARB No. 51 to establish accounting and reporting standards for the non-controlling interest in a subsidiary and the deconsolidation of a subsidiary; (b) changes the way the consolidated income statement is presented; (c) establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation; (d) requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated; and (e) requires expanded disclosures in the consolidated financial statements that clearly identify and distinguish between the interests of the parent's owners and the interests of the non-controlling owners of a subsidiary. SFAS No. 160 must be applied prospectively; however, the presentation and disclosure requirements must be applied retrospectively to provide comparability in the financial statements. Early adoption is prohibited. SFAS No. 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The Company reviewed the impact on its financial statements and does not believe that the adoption of this standard will have a significant impact on the Company's consolidated financial position, results of operations and cash flows.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities. The statement amends SFAS No. 133 and requires enhanced disclosures about an entity's derivative and hedging activities and thereby improves the transparency of financial reporting. The statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early adoption encouraged. The Company reviewed the impact on its financial statements and does not believe that the adoption of this standard will have a significant impact on the Company's consolidated financial position, results of operations and cash flows.

In April 2008, the FASB issued FASB Staff Position (“FSP”) SFAS 142-3, Determination of the Useful Life of Intangible Assets. This FSP amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, Goodwill and Other Intangible Assets. The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141(R), Business Combinations, and other U.S. generally accepted accounting principles (GAAP). This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. The Company reviewed the impact on its financial statements and does not believe that the adoption of this standard will have a significant impact on the Company's consolidated financial position, results of operations and cash flows.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles. SFAS No. 162 identifies the sources of accounting principles and the framework for selecting principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. This statement is effective as of November 15, 2008. The Company has adopted this standard with no impact on the Company's consolidated financial position, results of operations and cash flows.

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## CRITICAL ACCOUNTING ESTIMATES

Management's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities. Management evaluates its estimates on an on-going basis. Estimates are based on historical experience and on other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. There were no material changes to estimates in 2008.

The Company's critical accounting estimates are identified below:

### Allowance for Uncollectible Accounts:

Accounts receivable is comprised of balances due from customers net of estimated allowances for uncollectible accounts. In determining allowances, historical collection experience, current trends, aging of accounts receivable, and periodic credit evaluations of customers' financial condition are analyzed to arrive at appropriate allowances. Allowance levels change as customer-specific circumstances and the other analysis areas noted above change.

### Inventory Valuation:

The Company uses certain estimates and judgments to value inventory. Inventory is recorded at the lower of cost or market. The Company reviews its inventories for excess or obsolete products or components. Based on an analysis of historical usage, management's evaluation of estimated future demand, market conditions and alternative uses for possible excess or obsolete parts, carrying values are adjusted. For all inventory, the carrying value is reduced regularly to reflect the age and current anticipated product demand. If actual demand differs from the estimates, additional reductions would be necessary in the period such determination is made. The Company's reserve for excess or obsolete products or components as of year end 2008 was \$8.7 million. Excess and obsolete inventory is periodically disposed of through sale to third parties, scrapping or other means, and the reserves are appropriately reduced.

### Long-lived Assets:

The Company reviews long-lived assets by asset group for impairment whenever events or changes in circumstances indicate that the related carrying amounts may not be recoverable. Determining whether impairment has occurred typically requires various estimates and assumptions, including determining which cash flows are directly related to the potentially impaired asset, the amount and useful life over which cash flows will occur and the asset's residual value, if any. In turn, measurement of an impairment loss requires a determination of fair value, which is based on the best information available given the Company's historical experience and internal business plans.

### Business Combinations:

The Company has followed the guidance under SFAS No. 141, Business Combinations. The acquisition purchase price is allocated to the assets acquired and liabilities assumed based upon their respective fair values and subject to change during the twelve month period subsequent to the acquisition date. The Company utilizes management estimates and an independent third-party valuation firm to assist in determining the fair values of assets acquired and liabilities assumed. Such estimates and valuations require the Company to make significant assumptions, including projections of future events and operating performance.

### Goodwill:

The Company follows the guidance under SFAS No. 142, Goodwill and Other Intangible Assets, to record goodwill. Goodwill is not amortized; however it is tested at the reporting unit level for impairment annually or more frequently whenever events or changes in circumstances indicate that there may be impairment. Reporting units are operating segments or one level below, known as components, which can be aggregated for testing purposes. The Company has determined its components meet the aggregation criteria and as a result, goodwill is allocated to the Company's reporting units, Water Systems and Fueling Systems for testing. In assessing the recoverability of goodwill (i.e.,

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impairment testing), the Company looks at both the market valuation approach, where the Company's current and projected financial results are compared to entities of similar size and industry to determine the market value of the Company, and the cash flow approach which requires assumptions regarding estimated future cash flows and other factors to determine the fair value of the respective assets. Such cash flows consider factors such as expected future operating income and historical trends, as well as the effects of demand and competition. If the Company's assumptions and estimates change whereby fair value of the reporting units is below their associated carrying values, the Company may be required to record impairment. Goodwill included on the balance sheet as of year end 2008 was \$148.1 million. During the first period of the fourth quarter of 2008, the Company completed its annual impairment test of goodwill and determined there was no impairment. A 10 percent decrease in the fair value estimates used in the fourth quarter 2008 impairment test would not have changed this determination. This sensitivity analysis required the use of judgment and numerous subjective assumptions, which, if actual experience varies, could result in material differences in the requirements for impairment charges. Further, an extended downturn in the economy may impact certain components of the operating segments more significantly and could result in changes to the aggregation assumptions and impairment determination.

Significant judgment is required to determine if an indicator of impairment has taken place. Factors to be considered include; adverse change in operating results, decline in strategic business plans, significantly lower future cash flows, and sustainable decline in market data such as market capitalization. Given the changing economic conditions during the fourth quarter of 2008, the Company experienced a decline in its market capitalization. As of January 3, 2009, market capitalization was \$650 million compared to book value of \$349 million. SFAS No. 142 requires the performance of an interim goodwill impairment test if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The Company evaluated the move in its stock price, along with the Company's fourth quarter performance, and industry outlook. Based on this evaluation, the Company concluded that it did not have a triggering event in the fourth quarter that would require the performance of an interim goodwill impairment test.

#### Income Taxes:

Under the requirements of SFAS No. 109, Accounting for Income Taxes, the Company records deferred tax assets and liabilities for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The Company operates in multiple tax jurisdictions with different tax rates, and determines the allocation of income to each of these jurisdictions based upon various estimates and assumptions. In the normal course of business the Company will undergo tax audits by various tax jurisdictions. Such audits often require an extended period of time to complete and may result in income tax adjustments if changes to the allocation are required between jurisdictions with different tax rates. Although the Company has recorded all probable income tax contingencies in accordance with FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes and SFAS No. 109, Accounting for Income Taxes, these accruals represent estimates that are subject to the inherent uncertainties associated with the tax audit process, and therefore include contingencies. Management judgment is required in determining the Company's provision for income taxes, deferred tax assets and liabilities, which, if actual experience varies, could result in material adjustments to deferred tax assets and liabilities. The Company's operations involve dealing with uncertainties and judgments in the application of complex tax regulations in multiple jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits.

#### Pension and Employee Benefit Obligations:

With the assistance of the Company's actuaries, the discount rate used to determine pension and post-retirement plan liabilities is selected using a yield-curve approach. The yield-curve approach discounts each expected cash flow of the liability stream at an interest rate based on high quality corporate bonds. The present value of the discounted cash

flows is summed and an equivalent weighted-average discount rate is calculated. Market conditions have caused the discount rate to move from 6.40 percent last year to 6.90 percent this year. A change in the discount rate selected by the Company of 25 basis points would result in a change of about \$0.1 million of employee benefit expense. The Company consults with actuaries, asset allocation consultants and investment advisors in making its determination of the expected long-term rate of return on plan assets. Using input from these consultations such as long term investment sector expected returns, the correlations and standard deviations thereof, and the plan asset

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allocation, the Company has assumed an expected long-term rate of return on plan assets of 8.5 percent as of 2007. This is the result of stochastic modeling showing the 50th percentile median return at or above 8.5 percent. A change in the long-term rate of return selected by the Company of 25 basis points would result in a change of about \$0.3 million of employee benefit expense.

#### Stock-Based Compensation:

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123(R), Share-Based Payment. The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model with a single approach and amortized using a straight-line attribution method over the option's vesting period. Options granted to retirement eligible employees are immediately expensed. The Company uses historical data to estimate the expected volatility of its stock; the weighted average expected life; the period of time options granted are expected to be outstanding; and its dividend yield. The risk-free rates for periods within the contractual life of the option are based on the U.S. Treasury yield curve in effect at the time of the grant.

#### FACTORS THAT MAY AFFECT FUTURE RESULTS

This annual report on Form 10-K contains certain forward-looking information, such as statements about the Company's financial goals, acquisition strategies, financial expectations including anticipated revenue or expense levels, business prospects, market positioning, product development, manufacturing re-alignment, capital expenditures, tax benefits and expenses, and the effect of contingencies or changes in accounting policies. Forward-looking statements are typically identified by words or phrases such as "believe," "expect," "anticipate," "intend," "estimate," "may increase," "may fluctuate," "plan," "goal," "target," "strategy," and similar expressions or future or conditional verbs such as "may," "will," "should," "would," and "could." While the Company believes that the assumptions underlying such forward-looking statements are reasonable based on present conditions, forward-looking statements made by the Company involve risks and uncertainties and are not guarantees of future performance. Actual results may differ materially from those forward-looking statements as a result of various factors, including general economic and currency conditions, various conditions specific to the Company's business and industry, new housing starts, weather conditions, market demand, competitive factors, changes in distribution channels, supply constraints, technology factors, litigation, government and regulatory actions, the Company's accounting policies, future trends, and other risks, all as described in Item 1A and Exhibit 99.1 of this Form 10-K. Any forward-looking statements included in this Form 10-K are based upon information presently available. The Company does not assume any obligation to update any forward-looking information.

#### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is subject to market risk associated with changes in foreign currency exchange rates and interest rates. Foreign currency exchange rate risk is mitigated through several means: maintenance of local production facilities in the markets served, invoicing of customers in the same currency as the source of the products, prompt settlement of inter-company balances utilizing a global netting system and limited use of foreign currency denominated debt.

The results of operations are exposed to changes in interest rates primarily with respect to borrowings under the Company's revolving credit agreement (credit facility), where interest rates are tied to the prime rate or London Interbank Offered Rates (LIBOR). The average interest rate associated with borrowings against the credit facility paid by the Company in 2008 was 3.3 percent. As of January 3, 2009, the Company had \$35.0 million in outstanding borrowings under the Agreement. Based on the Company's variable rate debt at January 3, 2009, a hypothetical 1.0 percent increase in interest rates would have resulted in an annual increase in interest expense of approximately \$0.1 million. The Company does not, as a matter of policy, enter into derivative contracts for speculative purposes.

The interest rate swap agreement entered into by the Company on September 24, 2003, had a notional amount of \$10.0 million under which the Company received a fixed rate of interest of 6.3 percent and paid interest at a variable rate based on a three month LIBOR rate plus a spread. The average rate associated with the swap agreement paid by

the Company in 2008 was 5.8 percent. The fixed-to-variable interest rate swap was accounted for as a fair value hedge, per SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, with effectiveness assessed based on changes in the fair value of the underlying debt using incremental borrowing rates currently available on loans with similar terms and maturities. The effective gain or loss on the interest rate swap and that of the underlying debt were equal and offsetting resulting in no net effect to earnings. The swap contract matured on November 10, 2008 and was not renewed.

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## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

CONSOLIDATED STATEMENTS OF INCOME  
FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES

(In thousands, except per share amounts)

	2008	2007	2006
Net sales	\$ 745,627	\$ 602,025	\$ 557,948
Cost of sales	518,702	429,205	366,391
Gross profit	226,925	172,820	191,557
Selling, general and administrative expenses	147,987	119,748	102,478
Restructuring expenses	2,228	3,898	-
Operating income	76,710	49,174	89,079
Interest expense	(10,968)	(8,147)	(3,373)
Other income	1,289	3,010	1,791
Foreign exchange income/(loss)	5	80	(64)
Income before income taxes	67,036	44,117	87,433
Income taxes	22,925	15,434	30,671
Income from continuing operations	44,111	28,683	56,762
Discontinued operations	-	-	381
Income taxes	-	-	145
Income from discontinued operations	-	-	236
Net income	\$ 44,111	\$ 28,683	\$ 56,998
Income per share:			
Basic continuing operations	\$ 1.92	\$ 1.24	\$ 2.49
Basic discontinued operations	-	-	0.01
	\$ 1.92	\$ 1.24	\$ 2.50
Diluted continuing operations	\$ 1.90	\$ 1.22	\$ 2.43
Diluted discontinued operations	-	-	0.01
	\$ 1.90	\$ 1.22	\$ 2.44
Dividends per common share	\$ 0.50	\$ 0.47	\$ 0.43

See Notes to Consolidated Financial Statements.



CONSOLIDATED BALANCE SHEETS  
FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES

(In thousands)

	2008	2007
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 46,934	\$ 65,252
Receivables, less allowances of \$2,091 and \$2,594, respectively	68,048	64,972
<b>Inventories:</b>		
Raw material	67,785	57,958
Work-in-process	15,204	17,128
Finished goods	105,496	99,974
LIFO reserve	(18,612)	(18,914)
	169,873	156,146
Deferred income taxes	16,511	17,127
Other current assets	16,294	5,982
Total current assets	317,660	309,479
<b>Property, plant and equipment, at cost</b>		
Land and buildings	79,284	64,350
Machinery and equipment	172,706	161,280
Furniture & Fixtures	13,807	12,595
Other	11,556	16,909
	277,353	255,134
Less allowance for depreciation	(132,818)	(120,203)
	144,535	134,931
Intangible assets	75,737	66,925
Goodwill	148,082	140,034
Other assets	8,043	10,868
Total assets	\$ 694,057	\$ 662,237

## LIABILITIES AND SHAREOWNERS' EQUITY

Current liabilities:		
Accounts payable	\$ 24,505	\$ 27,986
Accrued expenses	47,991	46,085
Income taxes	8,239	6,180
Current maturities of long-term debt and short-term borrowings		
	677	10,398
Total current liabilities	81,412	90,649
Long-term debt	185,528	151,287
Deferred income taxes	4,161	11,686
Employee benefit plan obligations	69,142	24,713
Other long-term liabilities	4,877	5,358
Shareowners' equity:		
Common stock (65,000 shares authorized, \$.10 par value)		
outstanding (23,018 and 23,091, respectively)	2,302	2,309
Additional capital	113,397	105,428
Retained earnings	271,274	246,324
Accumulated other comprehensive income/(loss)	(38,036)	24,483
Total shareowners' equity	348,937	378,544
Total liabilities and shareowners' equity	\$ 694,057	\$ 662,237