FLOWSERVE CORP
Form 10-K
March 01, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006**

OR

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

Commission file number 1-13179

FLOWSERVE CORPORATION

(Exact name of registrant as specified in its charter)

New York	**31-0267900**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
5215 N. O Connor Boulevard Suite 2300, Irving, Texas	**75039**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code:
(972) 443-6500

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

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $1.25 Par Value	New York Stock Exchange

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

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

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 o No þ

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 þ No o

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. þ

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 þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company. Yes o No þ

The aggregate market value of the common stock held by non-affiliates of the registrant, computed by reference to the closing price of the registrant s common stock as reported on June 30, 2006 (the last business day of the registrant s most recently completed second fiscal quarter), was approximately $2,010,083,768. For purposes of the foregoing calculation only, all directors, executive officers and known 5% beneficial owners have been deemed affiliates.

Number of the registrant s common shares outstanding as of February 16, 2007 was 56,657,523.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the definitive proxy statement for the registrant s Annual Meeting of Shareholders to be held on May 17, 2007 is incorporated by reference into Part III hereof.

FLOWSERVE CORPORATION

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PART I

ITEM 1. *BUSINESS.*

GENERAL

Flowserve Corporation is a world leading manufacturer and aftermarket service provider of comprehensive flow control systems. Unless the context otherwise indicates, references herein to Flowserve, the Company and such words as we, our and us include Flowserve Corporation and its subsidiaries. We were incorporated in the State of New York on May 1, 1912. We develop and manufacture precision-engineered flow control equipment, such as pumps, valves and seals, for critical service applications that require high reliability. We use our manufacturing platform to offer a broad array of aftermarket equipment services, such as installation, advanced diagnostics, repair and retrofitting.

We sell our products and services to more than 10,000 companies, including some of the world s leading engineering and construction firms, original equipment manufacturers (OEMs), distributors and end users. Our products and services are used in several distinct industries across a broad geographic reach. Our bookings mix by industry in 2006 consisted of:

oil and gas	43 %
chemical	15 %
general industrial	23 %
power generation	13 %
water treatment	6 %

The breakdown of the geographic regions in which our sales were originated in 2006 were as follows:

North America	37 %
Europe	26 %
Middle East and Africa	16 %
Asia Pacific	15 %
Latin America	6 %

We have pursued a strategy of industry diversity and geographic breadth to mitigate the impact on our business of an economic downturn in any one of the industries or in any one part of the world we serve. For information on our sales and long-lived assets by geographic areas, see Note 17 to our consolidated financial statements included in this Annual Report.

We conduct our operations through three business segments:

Flowserve Pump Division (FPD) for engineered pumps, industrial pumps and related services;

Flow Control Division (FCD) for industrial valves, manual valves, control valves, nuclear valves, valve actuators and controls and related services; and

Flow Solutions Division (FSD) for precision mechanical seals and related services.

FINANCIAL INFORMATION ABOUT SEGMENTS AND GEOGRAPHIC AREAS

In addition to the information presented below, Note 17 Business Segment Information of the notes to our consolidated financial statements contains additional information about our business segments and geographic areas in which we have conducted business for fiscal years 2006, 2005 and 2004.

FLOWSERVE PUMP DIVISION

Through FPD, we design, manufacture, distribute and service engineered and industrial pumps and pump systems, replacement parts and related equipment, principally to industrial markets. FPD s products and services are primarily used by companies that operate in the oil and gas, chemical processing, power generation, water

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treatment and general industrial markets. Our pump systems and components are currently manufactured at 27 plants worldwide, of which 9 are located in North America, 11 in Europe and 7 in South America and Asia. We also manufacture a small portion of our pumps through several foreign joint ventures. We market our pump products through our worldwide sales force and our regional service and repair centers or through independent distributors and sales representatives.

In June 2006, Flowserve entered into a joint venture agreement with the Al Rashaid Group to build the largest original pump equipment service and repair and learning center facility in Saudi Arabia. In addition to service and repair, the facility will have the capability to engineer, assemble and test new and upgraded pumping equipment. Construction of the 20,500 square meter (220,660 square feet) complex will be located at the Al Rashaid Oil Field Center in Dhahran, Saudi Arabia and is expected to be completed by end of 2007.

In December 2006, Flowserve acquired the assets of Canada Alloy Castings. The business will be integrated into Flowserve Pumps, but will continue to operate under the name Canada Alloy Castings (CAC). CAC specializes in large alloy castings, up to 35,000 lbs gross weight. CAC provides Flowserve with a secure source of supply and will support future FPD growth. We also expect significantly shortened lead times on critical castings supplied by CAC.

FPD Products

We manufacture more than 150 different active pump models, ranging from simple fractional horsepower industrial pumps to high horsepower engineered pumps (greater than 30,000 horsepower). Our pumps are manufactured in a wide range of metal alloys and with a variety of configurations, including pumps that utilize mechanical seals (sealed pumps) and pumps that do not utilize mechanical seals (magnetic-drive and other pumps).

The following is a summary list of our pump products and globally recognized brands:

FPD Product Types

Centrifugal Pumps	Positive Displacement Pumps	Specialty Products & Systems
Chemical Process ANSI and ISO	Reciprocating	Hydraulic Decoking Systems
Petroleum Process API 610	Gear	Reactor Recycle Systems
Horizontal Between Bearing Single stage	Twin Screw	Cryogenic Liquid Expander
Horizontal Between Bearing Multi stage		
Vertical		
Submersible Motor		
Nuclear		

FPD Brand Names

ACEC	Cameron
Byron Jackson	Duriron
Durco	IDP
Flowserve	Pleuger
Pacific	Sier-Bath
Scienco	United Centrifugal
Worthington-Simpson	Wilson-Snyder
Western Land Roller	Jeumont-Schneider

Worthington Aldrich	TKL

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FPD Services

We provide engineered aftermarket services through our global network of 50 service centers in 20 countries. Our FPD service personnel provide a comprehensive set of equipment maintenance services for flow management control systems, including repair, advanced diagnostics, installation, commissioning, re-rate and retrofit programs, machining and full service solution offerings. A large portion of our FPD service work is performed on a quick response basis, and we offer 24-hour service in all of our major markets.

FPD New Product Development

Our investments in new product research and development have consistently led to the production of more reliable and higher efficiency pump designs. In line with our end-user strategy, the majority of our new FPD products and enhancements are driven by our customers need to achieve higher production rates at lower costs. As a result, we continually collaborate with our customers in developing advanced technical solutions to improve the availability and productivity of their pumping systems. This type of technology advancement is best demonstrated by our recent release of the IPS Tempo product. The flagship of our *Intelligent Pumping Series*, IPS Tempo is a product developed and designed to incorporate our operating intelligence and protection logic in the control of pumps installed at unmanned locations. Much of our new product development is applied to projects where customer funding is available to support the investment. In addition, several of our new technology initiatives are partially funded by third parties including:

Subsea Multiphase pumping project where a highly specialized twin screw pump manufactured by our Brantford Canada facility is joined to a submersible motor manufactured by our Hamburg Germany facility for positioning on the sea floor and recovery of oil reserves from abandoned wells. An example of Flowserve technology applied to solving oil shortage problems.

Pipeline Research Council Institute technology advancement project where we are attempting to redefine the performance characteristic of pipeline pumps reducing wasted energy at off design operating points. Flowserve technology applied to improving profitability to pipeline customers.

High Pressure Water Injection project where we are developing a product for an enhanced oil recovery project requiring pressures in excess of 7500 psig (520 bar). Flowserve expertise in hydraulic design, mechanical design and materials technology is being applied to solve the problems associated with this extremely complex customer application on an off shore platform.

In addition to Product and Technology development, FPD Research and Development personnel continue to support many of the organizations leading the industry (HI, API, ISO, Europump) and have been recognized as leaders in pump technology. Bruno Schiavello, our hydraulics specialist, has been recently awarded the prestigious 2006 ASME Fluids Machinery Design Award for his many years of service in the fluids design discipline.

FPD Customers

FPD s customer mix is diversified, including leading engineering procurement and construction firms, OEMs, distributors and end users. Our sales mix of original equipment products and aftermarket services diversifies our business and somewhat mitigates the impact of economic cycles in our business.

FPD Competition

The pump industry is highly fragmented, with more than 100 competitors. We compete, however, primarily against a relatively limited number of large companies operating on a global scale. Competition is generally based on price, expertise, delivery times, breadth of product offerings, contractual terms, previous installation history and reputation for quality. Some of our largest pump industry competitors include ITT Industries, Ebara Corporation, KSB Inc., The Weir Group PLC, Sulzer Pumps and United Technologies Corporation.

The pump industry has undergone considerable consolidation in recent years, primarily caused by (1) the need to lower costs through reduction of excess capacity and (2) customers preference to align with global full service suppliers in simplifying their supplier base. Despite the consolidation activity, the market remains highly

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competitive. We believe that we are the largest pump manufacturer serving the oil, chemical and power generation industries, and the third largest pump manufacturer overall. We believe that our broad range of pumps for the oil, power and chemical industries, our strong customer relationships and more than 100 years of experiences in pumping equipment, and our reputation for providing quality engineering solutions are our major sources of competitive advantage.

FPD Backlog

FPD s backlog of orders at December 31, 2006 was $1.3 billion, compared with $703.5 million on December 31, 2005. We expect to ship approximately 85% of our FPD backlog as of December 31, 2006 during 2007.

FLOW CONTROL DIVISION

FCD, the second largest business segment within Flowserve, designs, manufactures and distributes a broad portfolio of industrial valve products, including actuators, controls and related equipment. In addition, FCD leverages its experience and application know-how by offering a complete menu of engineered services to complement its expansive product portfolio. Valve products, used to direct the flow of liquids and gases, are an integral part of any flow control system. Typically, our valve products are customized, being engineered to perform specific functions within each of our customer s unique flow control environments.

Our products are primarily used by companies that operate in the chemical, power generation, oil and gas and general industries including water, mining and pharmaceutical. We produce the vast majority of our products at 20 principal manufacturing facilities, with only 5 of the 20 plants located in the United States. A small portion of our valves are produced through foreign joint ventures.

FCD Products

Together, our valve, actuator and automated valve accessory offerings represent one of the most comprehensive product portfolios in the flow control industry. Our valves are used in a wide variety of applications, from the more customary general service operations to the most extreme of environments, involving high degrees of corrosion, temperatures and or pressures. FCD s smart valve technologies, which integrate high technology sensors, microprocessor controls and digital positioners into a high performance control valve, permit real time system analysis, system warnings and remote services. These smart valve technologies are in response to the growing demand for increased automation, improved process control efficiency and digital communications at the plant level. We are committed to further enhancing the quality of our product portfolio by continuing to upgrade our existing offerings with cutting-edge digital technologies.

The following is a summary list of our generally available valve products and globally recognized brands:

FCD Product Types

Actuators and Accessories
Control Valves
Ball Valves
Lubricated Plug Valves
Pneumatic Positioners
Electro Pneumatic Positioners
Smart Valves
Digital Communications
Manual Quarter-Turn Valves
Valve Automation Systems
Valve/Actuator Software
Nuclear Valves
Quarter-Turn Actuators
Valve Repair Services

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FCD Brand Names

Accord	NAF
Anchor/Darling	NAVAL
Argus	Noble Alloy
Atomac	Norbro
Automax	Nordstrom
Battig	PMV
Durco	P+W
Edward	Serck Audco
Gestra	Schmidt Armaturen
Kammer	Valtek
Limitorque	Vogt
McCANNA/MARPAC	Worcester Controls

FCD Services

We provide aftermarket services through our network of 17 service centers located throughout the world. Our service personnel provide a comprehensive set of equipment maintenance services for flow control systems, including advanced diagnostics repair, installation, commissioning, retrofit programs and field machining capabilities. A large portion of our service work is performed on a quick response basis, including 24-hour service in all of our major markets. We believe our ability to offer these types of services provides us with a unique competitive advantage and unparalleled access to our customers installed base of flow control products.

FCD New Product Development

Our research and development investment has been targeted in areas that will advance our technological leadership and further differentiate our competitive advantage from a product perspective. The investment priority has been focused on significantly enhancing the digital integration and interoperability of the valve top works (positioners, actuators, limit switches, and associated accessories) with Distributed Control Systems (DCS). Our efforts in this area continue to pursue the development and deployment of next-generation hardware and software for valve diagnostics, and the integration of the resulting device intelligence through the DCS to provide a practical and effective asset management capability for the end-user. In addition to developing these new capabilities and value-added services, our investments also include product portfolio expansion and fundamental research in material sciences in order to increase the temperature, pressure, and erosion-resistance limits of existing products. These investments are made by adding new resources and talent to the organization, as well as leveraging the experience of FPD and FSD, and increasing our collaboration with third parties. We expect to continue our research and development investments in the areas mentioned above.

FCD Customers

FCD s customer mix spans across several industries, including the chemical, petroleum, power, water and general industries. FCD s product mix includes original equipment, aftermarket parts and services.

FCD Competition

While in recent years the valve market has undergone a significant amount of consolidation, in relative terms, the market remains highly fragmented. Some of the largest valve industry competitors include Crane Co., Dresser Inc., Emerson, Kitz and Tyco.

Our assessments show that the top 10 global valve manufacturers collectively comprise approximately 30% of the valve market. Based on independent industry sources we believe that we are the third largest industrial valve supplier on a global basis. We believe that our comprehensive portfolio of valve products and services, our focus on

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execution and our competency in severe corrosion and erosion applications are key sources of our competitive advantage.

FCD Backlog

FCD s backlog of orders at December 31, 2006 was $314.3 million, compared with $240.6 million on December 31, 2005. We expect to ship approximately 93% of our backlog on December 31, 2006 during 2007.

FLOW SOLUTIONS DIVISION

Through FSD, we design, manufacture and distribute mechanical seals, sealing systems and parts, and provide related services, principally to process industries. Rotating equipment containing mechanical seals require replacement throughout the products useful lives. The replacement of mechanical seals is an integral part of our aftermarket services. Our mechanical seals are used on a variety of rotating equipment, including pumps, mixers, compressors, steam turbines and other specialty equipment, primarily in the petroleum, natural gas, chemical processing, mineral and ore processing and general industrial end-user markets.

We manufacture mechanical seals at four plants in the U.S. and at five plants outside the U.S. Through our global network of 67 Quick Response Centers (QRCs), we provide service, repair and diagnostic services for maintaining components of flow control systems. Our mechanical seal products are primarily marketed to end users through our direct sales force and, on a commission basis, to distributors and sales agents. A portion of our mechanical seal products is sold directly to original equipment manufacturers (OEMs) for incorporation into rotating equipment requiring mechanical seals.

FSD Products

We design, manufacture and distribute approximately 210 different models of mechanical seals and sealing systems. We believe our ability to deliver engineered new seal product orders within 72 hours from the customer s request through design, engineering, manufacturing, testing and delivery provides us with a leading competitive advantage. Mechanical seals are critical to the reliable operation of rotating equipment for prevention of leakage and emissions of hazardous substances and the reduction of shaft wear caused by non-mechanical seals. We also manufacture a gas-lubricated mechanical seal that is used in high-speed compressors for gas pipelines and in the oil and gas production and process markets. We continually update our mechanical seals and sealing systems to integrate emerging technologies.

The following list summarizes our seal products and services and globally recognized brands:

FSD Product Types

- Cartridge Seals
- Dry-Running Seals
- Metal Bellow Seals
- Elastomeric Seals
- Slurry Seals
- Split Seals
- Gas Barrier Seals
- Couplings
- Service and Repair
- Accessories and Support Systems
- Monitoring and Diagnostics

FSD Brand Names

BW Seals	GASPAC
Durametallic	Interseal
Five Star Seal	Pacific Wietz
Flowserve	Pac-Seal
Flowstar	QRC™

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FSD Services

We provide aftermarket services through our network of 67 QRCs located throughout the world, including 24 sites in North America. We also provide asset management services and condition monitoring for rotating equipment. Approximately 75% of our service work is performed on a quick-response basis, and we offer 24-hour service in all of our major markets.

FSD New Product Development

Our investments in new product research and development focus on developing longer lasting and more efficient products and value-added services. Approximately 30% of our original equipment mechanical seal sales for 2006 consisted of products developed within the past five years. In addition to numerous product upgrades, our recent mechanical seal and seal system innovations include: (1) low valve project seal; (2) batch chemical process seal; (3) improved split seal for water markets; (4) pump systems; and (5) expanded mineral and ore processing seal line.

We also market Flowstar.Net, an interactive tool used to actively monitor and manage information relative to equipment performance. Flowstar.Net enhances our customers ability to make informed decisions and respond quickly to plant production problems, extends the life of their production equipment and lowers maintenance expenses. This data has been expanded to include applications for developing new products and assisting in field applications.

None of these newly developed seal products required the investment of a material amount of our assets or was otherwise material.

FSD Customers

Our mechanical seal products and systems are sold directly to end users and to OEMs for incorporation into pumps, compressors, mixers or other rotating equipment requiring mechanical seals. Our mechanical seal sales are diversified among several industries, including petroleum, natural gas, chemical, mineral and ore processing and general industries.

FSD Competition

We compete against a number of manufacturers in the sale of mechanical seals. Among our largest global mechanical seal competitors are John Crane, a unit of Smiths Group Plc. and Eagle Burgmann, Inc., which is a joint venture of two traditional global seal manufacturers, Chesterton and AES. Based on independent industry sources, we believe that we are the second largest industrial mechanical seals supplier in the world. Our ability to quickly manufacture customers requests for engineered seal products, from design to engineering, manufacturing, testing and delivery, is a major competitive advantage.

FSD Backlog

FSD s backlog of orders at December 31, 2006 was $74.4 million, compared with $61.2 million at December 31, 2005. We expect to ship approximately 79% our backlog on December 31, 2006 during 2007.

GENERAL BUSINESS

Competition

Despite the consolidation trend over the past 10 years, the markets for our products are fragmented and highly competitive, with competition occurring on the basis of price, technical expertise, timeliness of delivery, contractual terms, previous installation history and reputation for quality and reliability. Timeliness of delivery, quality and the proximity of service centers are important considerations for our aftermarket products and services. In geographic regions where we are positioned to provide a quick response, customers have traditionally relied on us, rather than our competitors, for aftermarket products relating to our highly engineered and customized products. However, aftermarket competition for standard products is very competitive, and price competition has generally been

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increasing due to supply availability. Price competition tends to be less significant for OEMs than aftermarket services and generally has been increasing. In the aftermarket portion of our service business, we compete against large and well-established national and global competitors and, in some markets, against regional and local companies who produce low cost replicators of spare parts. We also compete with in-house maintenance departments of our end user customers. In the sale of aftermarket products and services, we benefit from our large installed base of pumps, seals and valves, which require maintenance, repair and replacement parts. In the petroleum industry, the competitors for aftermarket services tend to be the customers own in-house capabilities. In other industries, except the nuclear power industry, the competitors for aftermarket services tend to be local independent repair shops and low cost replicators. We possess certain competitive advantages in the nuclear power industry due to our N Stamp, a prerequisite to serve customers in that industry, and our considerable base of proprietary knowledge.

Generally, our customers are attempting to reduce the number of vendors from which they purchase, thereby reducing the size and diversity of their inventory. Although vendor reduction programs could adversely affect our business, we have been successful in entering into global arrangements with a number of customers to leverage competitive advantages.

Our ability to use our portfolio of products and solutions to meet customer demands is a competitive strength. We continue to explore and develop potential new solutions, as well as products (pumps, valves, and seals), with our customers to improve service opportunities and increase our market share.

New Product Development

We spent approximately $29.7 million, $24.3 million and $25.2 million during 2006, 2005 and 2004, respectively, on research and development initiatives. Our research and development group consists of engineers involved in new product development and improvement of existing products. Additionally, we sponsor consortium programs for research with various universities and jointly conduct limited development work with certain vendors, licensees and customers. We believe current expenditures are adequate to sustain our ongoing research and development activities.

Customers

We sell to a wide variety of customers in the oil and gas, chemical, power generation, water treatment and general industries. No individual customer accounted for more than 5% of our consolidated 2006 revenues.

We are not required to carry unusually high amounts of inventory to meet customer delivery requirements. We have been working to increase our overall inventory efficiency to improve our operational effectiveness and to reduce working capital needs. We generally do not provide rights of product return for our customers and do not offer extended payment terms.

Selling and Distribution

We primarily distribute our products through direct sales by employees assigned to specific regions, industries or products. In addition, we use distributors and sales agents to supplement our direct sales force in countries where business practices or customs make it appropriate, or wherever it is not economical to have direct sales staff. We generate a majority of our sales leads through existing relationships with vendors, customers and prospects or through referrals.

Intellectual Property

We own a number of trademarks and patents relating to the name and design of our products. We consider our trademarks and patents to be an important aspect of our business. In addition, our pool of proprietary information, consisting of know-how and trade secrets related to the design, manufacture and operation of our products, is considered particularly important and valuable. Accordingly, we attempt to proactively protect such proprietary information. We generally own the rights to the products which we manufacture and sell and are unencumbered by any license or franchise to operate. Our trademarks can typically be renewed indefinitely as long as they remain in

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use, whereas our existing patents generally expire 20 years from the dates they were filed, which has occurred at various times in the past. We do not believe that the expiration of any individual patent(s) will have a material adverse impact on our operations.

Raw Materials

The principal raw materials used in manufacturing of our products are readily available and include bar stock and structural steel, castings, fasteners, gaskets, motors, silicon and carbon faces and fluoropolymer components. While substantially all raw materials are purchased from outside sources, we have been able to obtain an adequate supply and anticipate no shortages of such materials. We continue to expand worldwide sourcing to capitalize on low cost sources of purchased goods.

We are a vertically integrated manufacturer of certain pump and valve products. Certain corrosion-resistant castings for our pumps and quarter-turn valves are manufactured at our foundries. Other metal castings are either manufactured at our foundries or purchased from outside sources.

We also use highly engineered corrosion resistant plastic parts for certain pump and valve product lines. These include rotomolding as well as injection and compression molding of a variety of fluoropolymer and other plastic materials. We do not anticipate difficulty in obtaining raw materials in the future.

Suppliers of raw materials for nuclear markets must be qualified by the American Society of Mechanical Engineers and, accordingly, are limited in number. However, to date we have experienced no significant difficulty in obtaining such materials.

Employees and Labor Relations

We have approximately 14,000 employees globally. A portion of the hourly employees at our pump manufacturing plant located in Vernon, California, our pump service center located in Cleveland, Ohio, our valve manufacturing plant located in Lynchburg, Virginia and our foundry located in Dayton, Ohio, are represented by unions. Additionally, some employees at select facilities in the following countries are unionized or have employee works councils: Argentina, Australia, Austria, Belgium, Brazil, Canada, Finland, France, Germany, Italy, Japan, Mexico, the Netherlands, Spain, Sweden, Switzerland and the United Kingdom. We believe relations with our employees throughout our operations are generally satisfactory, including those employees represented by unions and works councils. No unionized facility produces more than 5% of our revenues. We entered into new multi-year collective bargaining agreements with our unions in Dayton, Ohio and Australia during 2006.

Environmental Regulations and Proceedings

We are subject to environmental laws and regulations in all jurisdictions in which we have operating facilities. These requirements primarily relate to the generation and disposal of solid and hazardous waste, air emissions and waste water discharges. We periodically make capital expenditures to abate and control pollution and to satisfy environmental requirements. At present, we have no plans for any material capital expenditures for environmental control equipment at any of our facilities. However, we have incurred and continue to incur operating costs relating to ongoing environmental compliance matters, although certain costs have been reduced by successful waste minimization programs. Based on existing and proposed environmental requirements and our anticipated production schedule, we believe that future environmental compliance expenditures will not have a material adverse effect on our financial position, results of operations or cash flows.

We use hazardous substances and generate hazardous wastes in many of our manufacturing and foundry operations. Most of our current and former properties are or have been used for industrial purposes and may require some clean-up of historical contamination. During the due diligence phase of our acquisitions, we conduct environmental site assessments in an attempt to determine any potential environmental liability and to identify the need for clean-up. We are currently conducting follow-up investigation and/or remediation activities at those locations where we have known environmental concerns. We have cleaned up a majority of the sites with known historical contamination and we are addressing the remaining identified issues.

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Over the years, we have been involved as one of many potentially responsible parties (PRP) at former public waste disposal sites that are or were subject to investigation and remediation. We are currently involved as a PRP at four Superfund sites. The sites are in various stages of evaluation by government authorities. Our total projected fair share cost allocation at all four of these sites is expected to be less than $100,000. See Item 3. Legal Proceedings for more information.

We have established reserves that we believe to be adequate to cover our currently identified on-site and off-site environmental liabilities.

Exports

Our export sales from the United States (U.S.) to foreign unaffiliated customers were $283.9 million in 2006, $221.6 million in 2005 and $275.6 million in 2004.

Licenses are required from U.S. government agencies to export certain products. In particular, products with nuclear applications are restricted, as are certain other pump, valve and mechanical seal products.

We are responding to an investigation by the U.S. Securities and Exchange Commission (SEC) relating primarily to products that two of our foreign subsidiaries delivered to Iraq from 1996 through 2003 under the United Nations Oil-for-Food Program. These two foreign subsidiaries have also been contacted by governmental authorities in their respective countries concerning their involvement in the United Nations Oil-for-Food Program. We engaged outside counsel in February 2006 to conduct an investigation of our foreign subsidiaries participation in the United Nations Oil-for-Food program. The outside counsel s investigation has found evidence to date that, during the years 2001 through 2003, certain non-U.S. personnel at the two foreign subsidiaries authorized payments in connection with certain of our product sales under the United Nations Oil-for-Food Program totaling approximately 0.6 million which were subsequently deposited by a third party into Iraqi-controlled bank accounts. These payments were not authorized under the United Nations Oil-for-Food Program and were not properly documented in the subsidiaries accounting records but were expensed as paid. We intend to continue to cooperate fully in the investigations by the SEC and foreign authorities which are ongoing. See Item 3. Legal Proceedings for more information.

We are continuing a process to determine our compliance posture with respect to U.S. export control laws and regulations and to disclose to the applicable U.S. governmental authorities, any past potential violations of the U.S. export control laws. See Item 3. Legal Proceedings for more information.

AVAILABILITY OF FORMS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION

Our shareholders may obtain, free of charge, copies of the following documents (and any amendments thereto) as filed with, or furnished, to the SEC as soon as reasonably practical after such material is filed with or furnished to the SEC: