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

FORM 10-Q

(Mark One)

☑ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2004**

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 No. 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 Blvd., Suite 2300, Irving Texas	**75039**
(Address of Principal Executive Offices)	(Zip code)

(972) 443-6500
(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant 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 ☐

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

As of April 21, 2006, there were 56,522,193 shares of the issuer's common stock outstanding.

FLOWSERVE CORPORATION
FORM 10-Q

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EXPLANATORY NOTE

As previously reported in our Annual Report on Form 10-K for the year ended December 31, 2004 ("2004 Annual Report"), we have restated our previously issued financial statements for 2002, 2003 and the first quarter of 2004. We refer to this restatement as the "2004 Restatement."

The condensed consolidated financial statements for the three months and nine months ended September 30, 2003 included in this Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2004 (the "Quarterly Report"), and all amounts referenced in this Quarterly Report for prior periods and prior period comparisons, are presented on a restated basis. For a description of the restatement, see Note 2 to the accompanying condensed consolidated financial statements and Note 2 to the consolidated financial statements included in our 2004 Annual Report.

As a result of the restatement and our obligations regarding internal controls under Section 404 of the Sarbanes-Oxley Act of 2002 ("Section 404"), we delayed filing this Quarterly Report and certain of our other periodic reports. Due to this delay and the significant changes we have made to our business in the interim, certain information presented herein relating to our business relates to certain events that occurred subsequent to September 30, 2004, including the restatement of our financial statements, disclosures regarding our internal controls and procedures and updates to legal proceedings.

On February 13, 2006, we filed our 2004 Annual Report and included therein our consolidated financial statements as of December 31, 2004 and for the year then ended and our restated consolidated financial statements as of December 31, 2003 and for the years ended December 31, 2003 and 2002. We did not amend our Annual Reports on Form 10-K or Quarterly Reports on Form 10-Q for periods affected by the restatement that ended on or prior to December 31, 2003, and the financial statements and related financial information contained in such reports should no longer be relied upon.

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended September 30,	
	2004	2003
(Amounts in thousands, except per share data)		(As restated)
Sales	**$ 652,134**	$ 555,955
Cost of sales	**458,313**	387,275
Gross profit	**193,821**	168,680
Selling, general and administrative expense	**152,395**	131,881
Integration expense	**—**	3,836
Operating income	**41,426**	32,963
Interest expense	**(21,161)**	(20,874)
Interest income	**669**	1,745
Loss on optional prepayments of debt	**(963)**	(369)
Other expense, net	**(4,107)**	(1,353)
Earnings before income taxes	**15,864**	12,112
Provision for income taxes	**9,909**	2,000
Income from continuing operations	**5,955**	10,112
Discontinued operations, net of tax	**413**	(238)
Net earnings	**$ 6,368**	$ 9,874
Earnings per share:		
Basic:		
Continuing operations	**$ 0.11**	$ 0.18
Discontinued operations	**0.01**	—
Net earnings	**$ 0.12**	$ 0.18
Diluted:		
Continuing operations	**$ 0.10**	$ 0.18
Discontinued operations	**0.01**	—
Net earnings	**$ 0.11**	$ 0.18

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Amounts in thousands)	Three Months Ended September 30, 2004	2003 (As restated)
Net earnings	**$ 6,368**	$ 9,874
Other comprehensive income (expense):		
Foreign currency translation adjustments, net of tax	**3,362**	(5,244)
Cash flow hedging activity, net of tax	**(4,840)**	1,081
Other comprehensive loss	**(1,478)**	(4,163)
Comprehensive income	**$ 4,890**	$ 5,711

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands, except per share data)	Nine Months Ended September 30, 2004	2003 (As restated)
Sales	**$ 1,905,760**	$ 1,721,324
Cost of sales	**1,335,359**	1,203,895
Gross profit	**570,401**	517,429
Selling, general and administrative expense	**448,175**	389,034
Integration expense	**—**	15,908
Restructuring expense	**—**	1,820
Operating income	**122,226**	110,667
Interest expense	**(60,988)**	(63,313)
Interest income	**1,230**	3,280
Loss on optional prepayments of debt	**(1,048)**	(1,008)
Other expense, net	**(8,916)**	(5,551)
Earnings before income taxes	**52,504**	44,075
Provision for income taxes	**33,696**	14,511
Income from continuing operations	**18,808**	29,564
Discontinued operations, net of tax	**975**	235
Net earnings	**$ 19,783**	$ 29,799
Earnings per share:		
Basic:		
Continuing operations	**$ 0.34**	$ 0.54
Discontinued operations	**0.02**	—
Net earnings	**$ 0.36**	$ 0.54
Diluted:		
Continuing operations	**$ 0.33**	$ 0.54
Discontinued operations	**0.02**	—
Net earnings	**$ 0.35**	$ 0.54

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Nine Months Ended September 30,	
	2004	2003
(Amounts in thousands)		(As restated)
Net earnings	**$ 19,783**	$ 29,799
Other comprehensive income (expense):		
Foreign currency translation adjustments, net of tax	**(10,951)**	32,655
Cash flow hedging activity, net of tax	**(4,433)**	687
Other comprehensive (loss) income	**(15,384)**	33,342
Comprehensive income	**$ 4,399**	$ 63,141

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except per share data)	September 30, 2004	December 31, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 40,483**	$ 53,522
Accounts receivable, net of allowance for doubtful accounts of $14,061 and $18,641	**500,828**	505,949
Inventories, net	**436,096**	412,374
Deferred taxes	**79,244**	64,585
Prepaid expenses and other	**31,472**	26,091
Total current assets	**1,088,123**	1,062,521
Property, plant and equipment, net of accumulated depreciation of $439,224 and $411,836	**431,831**	443,864
Goodwill	**872,271**	871,960
Deferred taxes	**20,941**	31,741
Other intangible assets, net	**160,694**	169,084
Other assets, net	**91,770**	101,342
Total assets	**$ 2,665,630**	$2,680,512
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**$ 267,669**	$ 250,614
Accrued liabilities	**312,920**	286,433
Debt due within one year	**70,636**	71,035
Total current liabilities	**651,225**	608,082
Long-term debt due after one year	**811,401**	879,766
Retirement obligations and other liabilities	**372,951**	370,201
Shareholders' equity:		
Serial preferred stock, $1.00 par value, 1,000 shares authorized, no shares issued	**—**	—
Common shares, $1.25 par value	**72,018**	72,018
Shares authorized — 120,000		
Shares issued — 57,614		
Capital in excess of par value	**471,505**	477,443
Retained earnings	**429,911**	410,128
	973,434	959,589
Treasury stock, at cost — 2,344 and 2,775 shares	**(52,676)**	(62,575)
Deferred compensation obligation	**6,675**	7,445
Accumulated other comprehensive loss	**(97,380)**	(81,996)
Total shareholders' equity	**830,053**	822,463
Total liabilities and shareholders' equity	**$ 2,665,630**	$2,680,512

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)	Nine Months Ended September 30, 2004	2003 (As restated)
Cash flows — Operating activities:		
Net earnings	**$ 19,783**	$ 29,799
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation	**46,650**	45,157
Amortization	**8,031**	7,873
Amortization of deferred loan costs and discount	**3,787**	3,745
Write-off of unamortized deferred loan costs and discount	**1,048**	1,008
Net loss on the disposition of assets	**314**	965
Impairment of assets	**—**	695
Restricted stock compensation expense	**735**	451
Change in assets and liabilities, net of acquisitions:		
Accounts receivable	**4,063**	67,262
Inventories	**(20,898)**	14,083
Prepaid expenses and other	**(5,625)**	3,003
Other assets	**381**	(13,553)
Accounts payable	**7,590**	(26,327)
Accrued liabilities and income taxes payable	**18,685**	(685)
Retirement obligations and other liabilities	**7,226**	(23,577)
Net deferred taxes	**(4,926)**	5,631
Net cash flows provided by operating activities	**86,844**	115,530
Cash flows — Investing activities:		
Capital expenditures	**(28,527)**	(19,117)
Cash received for disposal of assets	**4,093**	2,207
Cash paid for acquisition	**(9,429)**	—
Net cash flows used by investing activities	**(33,863)**	(16,910)
Cash flows — Financing activities:		
Net (repayments) borrowings under lines of credit	**(355)**	5,339
Payments on long-term debt	**(152,480)**	(125,000)
Proceeds from issuance of long-term debt	**85,000**	—
Payment of deferred loan costs	**(665)**	(1,767)
Proceeds from sale of common shares	**2,487**	—
Net cash flows used by financing activities	**(66,013)**	(121,428)
Effect of exchange rate changes on cash	**(7)**	6,991
Net change in cash and cash equivalents	**(13,039)**	(15,817)
Cash and cash equivalents at beginning of year	**53,522**	48,991
Cash and cash equivalents at end of period	**$ 40,483**	$ 33,174

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Accounting Policies

Basis of Presentation

The accompanying condensed consolidated balance sheet as of September 30, 2004, and the related condensed consolidated statements of income and comprehensive income for the three and nine months ended September 30, 2004 and 2003, and the condensed consolidated statements of cash flows for the nine months ended September 30, 2004 and 2003, are unaudited. In management's opinion, all adjustments comprising normal recurring adjustments necessary for a fair presentation of such condensed consolidated financial statements have been made.

The accompanying condensed consolidated financial statements and notes in this Quarterly Report are presented as permitted by Regulation S-X and do not contain certain information included in our annual financial statements and notes to the financial statements. Accordingly, the accompanying condensed consolidated financial information should be read in conjunction with the restated consolidated financial statements for the year ended December 31, 2003 presented in our 2004 Annual Report, which was filed with the Securities and Exchange Commission ("SEC") on February 13, 2006.

Stock-Based Compensation

We have several stock-based employee compensation plans, which we account for under the recognition and measurement principles of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," and related interpretations. For 2004 and prior years, no stock-based employee compensation cost is reflected in net earnings for stock option grants, as all options granted under those plans had an exercise price equal to or in excess of the market value of the underlying common stock on the date of grant. Should we elect to modify any of our existing stock option awards, APB No. 25, as interpreted by Financial Accounting Standards Board ("FASB") Financial Interpretation ("FIN") No. 44, "Accounting for Certain Transactions Involving Stock Compensation," requires us to recognize the intrinsic value of the underlying options at the date the modification becomes effective. Modifications could include accelerated vesting, a reduction in exercise prices or extension of the exercise period.

Awards of restricted stock are valued at the market price of our common stock on the grant date and recorded as unearned compensation within shareholders' equity. The unearned compensation is amortized to compensation expense over the vesting period of the restricted stock. We have unearned compensation of $6.1 million and $0.9 million at September 30, 2004 and December 31, 2003, respectively. These amounts will be recognized into net earnings in prospective periods.

The following table illustrates the effect on net earnings and earnings per share if we had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," to all stock-based employee compensation, calculated using the Black-Scholes option-pricing model.

(Amounts in thousands, except per share data)	Quarter Ended September 30, 2004	2003 (As restated)
Net earnings, as reported	**$ 6,368**	$ 9,874
Restricted stock compensation expense (income) included in net earnings, net of related tax effects	**385**	172
Less: Stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	**(297)**	(1,233)
Pro forma net earnings	**$ 6,456**	$ 8,813
Net earnings per share — basic:		
As reported	**$ 0.12**	$ 0.18
Pro forma	**0.12**	0.16
Net earnings per share — diluted:		
As reported	**$ 0.11**	$ 0.18
Pro forma	**0.12**	0.16

(Amounts in thousands, except per share data)	Nine Months Ended September 30, 2004	2003 (As restated)
Net earnings, as reported	**$ 19,783**	$ 29,799
Restricted stock compensation expense (income) included in net earnings, net of related tax effects	**482**	296
Less: Stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	**(1,309)**	(2,407)
Pro forma net earnings	**$ 18,956**	$ 27,688
Net earnings per share — basic:		
As reported	**$ 0.36**	$ 0.54
Pro forma	**0.34**	0.50
Net earnings per share — diluted:		
As reported	**$ 0.35**	$ 0.54
Pro forma	**0.34**	0.50

The above pro forma disclosures may not be representative of effects for future years, since the determination of the fair value of stock options granted includes an expected volatility factor and additional option grants are expected to be made each year.

Other Accounting Policies

Our significant accounting policies, for which no significant changes have occurred in the quarter ended June 30, 2004, are detailed in Note 1 of our 2004 Annual Report.

Accounting Developments

Pronouncements Implemented

In December 2003, the FASB issued FIN No. 46(R), “Consolidation of Variable Interest Entities,” which addresses the consolidation of variable interest entities (“VIEs”) by business enterprises that are the primary beneficiaries. A VIE is an entity: 1) that does not have sufficient equity investment at risk to permit it to finance its activities without additional subordinated financial support, or 2) whose equity investors lack the characteristics of a controlling financial interest, or

3) whose equity investors have voting rights that are not proportionate to their economic interests, and the activities of the entity involve or are conducted on behalf of an investor with a disproportionately small voting interest. The primary beneficiary of a VIE is the enterprise that has the majority of the risks or rewards associated with the VIE. We believe we have no interests in VIEs that require disclosure or consolidation under FIN No. 46(R), and therefore its implementation had no significant effect on our consolidated results of operations or financial position.

Pronouncements Not Yet Implemented

In May 2004, the FASB issued FASB Staff Position ("FSP") No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003" (the "Medicare Act"). The Medicare Act provides for certain federal subsidies on drug benefits provided under retiree health plans. In the third quarter of fiscal 2004, we adopted FSP No. 106-2, retroactive to December 8, 2003, the date of the enactment of the Medicare Act. The expected subsidy reduced our accumulated postretirement benefit obligation by approximately $4.5 million, which we recognized as a reduction in the unrecognized net actuarial loss and will be amortized over the average remaining service life of the employees eligible for postretirement benefits. The adoption of FSP No. 106-2 did not have a material impact on our consolidated financial position or results of operations.

Although there are no other final pronouncements recently issued that we have not adopted and that we expect to impact reported financial information or disclosures, accounting promulgating bodies have a number of pending projects which may directly impact us. We continue to evaluate the status of these projects and as these projects become final, we will provide disclosures regarding the likelihood and magnitude of their impact, if any.

2. Restatement

For the errors discussed below, we restated our condensed consolidated financial statements for the three and nine months ended September 30, 2003 presented herein.

The following table sets forth the nature of significant restatement errors and their impact on the previously reported net earnings:

Summary of Restatement Issues Affecting Net Earnings
For the Three and Nine Months Ended September 30, 2003

(Amounts in thousands)	Three months ended September 30, 2003	Nine months ended September 30, 2003
Net earnings, as previously reported	$ 10,599	$ 32,067
Long-term contract accounting	(2,817)	(2,817)
Inventory valuation	(764)	1,505
Unclaimed property	(432)	(676)
Financial derivatives	(314)	(1,476)
Intercompany reconciliations	(239)	(1,808)
Pension expense	91	903
Fixed assets and intangibles	—	(863)
Other	27	723
Tax matters	3,723	2,241
Net earnings, as restated	$ 9,874	$ 29,799

Inventory Valuation — We corrected our financial statements for inconsistencies in the application of our accounting policy for obsolete and slow moving inventory, errors in our last-in, first-out ("LIFO") calculations, and errors in adjusting for lower-of-cost-or-market considerations. The inconsistencies related to (i) obsolete and slow moving inventory mainly resulting from limitations in our systems and processes that did not effectively identify excess inventory quantities; and (ii) the inventories of acquired businesses where our identification of slow moving items was not performed timely. The errors in LIFO and lower-of-cost-or-market resulted from inaccurate calculations.

Long-Term Contract Accounting — We identified one long-term contract that was accounted for using the percentage of completion method in which we did not include the estimated cost of the work performed by subcontractors as part of our total estimated costs in determining the percentage of completion accounting for the overall contract. We also identified a long-term contract in which costs related to the contracts were not recorded in the appropriate periods and resulted in corrections to cost of sales in prior periods.

Intercompany Reconciliations — Our accounting for intercompany transactions was adversely affected by information technology system conversions, acquisitions, and changes in corporate processes for recording intercompany transactions. Our initial analysis of intercompany transactions was expanded to include an assessment of intercompany balance differences at each of the reporting dates. Certain reconciling items were identified through this assessment that required adjustment to the consolidated statements of operations.

Pension Expense — As part of a comprehensive review of our pension plans, we identified errors in the accounting for non-U.S. pension plans. Certain plan obligations had not been measured at the actuarially determined present value, which resulted in errors in our annual pension expense and related liabilities.

Fixed Assets and Intangibles — As part of a comprehensive physical observation and assessment of fixed assets, we identified errors in our fixed asset processes related to disposals and abandonments that were not recorded in our accounting records necessitating adjustments to report the gains or losses on disposal in the appropriate periods. We also identified errors that resulted from not adjusting for the impact of purchase accounting within the general ledgers at certain locations of recently acquired businesses, amortization of leasehold improvements over periods in excess of the related lease terms, and errors in the amortization of intangible assets. These errors affected amounts reported for fixed assets, goodwill, other intangible assets, depreciation and amortization, loss on disposals, and foreign currency translation accounts.

Financial Derivatives — We identified errors in our accounting for financial derivatives related to foreign currency forward exchange contracts, which consisted of incorrectly recording unrealized gains and losses in other comprehensive loss for certain contracts that did not meet the criteria for hedge accounting. We also identified errors related to the recording of balances underlying the financial derivatives.

Unclaimed Property — We identified errors in accounting for unclaimed property primarily for unapplied cash and customer credits related to accounts receivable and for checks issued to vendors and to other payees that were not presented for payment. We previously recorded such items as income and removed these amounts from our balance sheet accounts. The correction reinstates such amounts within accrued liabilities as we began a process of filing with various states under voluntary disclosure agreements.

Other — We identified other errors as part of the restatement where the individual impact on net earnings was not as significant, which resulted from the following:

- errors in the original allocation of the purchase price for acquired businesses to property, plant and equipment, goodwill, accrued liabilities and deferred income taxes;
- errors in reconciliations of account balances;
- errors in accounting for equity investments that were based on foreign accounting standards rather than accounting principles generally accepted in the United States of America (“GAAP”); and
- other errors which were not deemed individually significant for separate disclosure.

Tax Matters — Due to significant employee turnover, information technology system limitations, corporate legal restructurings, several multinational acquisitions, and inadequate reconciliations, we identified errors in the amounts recorded in current and deferred income taxes. We undertook a process to identify our tax basis amounts, for both domestic and international locations, and performed a comprehensive review of our purchase accounting for recent acquisitions. This process included a detailed compilation of our book and tax differences at each of the reporting dates, as well as reconciliations of our income tax payable accounts to tax returns, as filed or as amended.

We also identified errors that occurred in applying purchase accounting to businesses acquired, including income tax liabilities arising in years prior to the acquisitions, which were corrected in the related balance sheet accounts. We also identified errors in our U.S. federal income tax returns filed for 1999 through 2001 as a result of an Internal Revenue Service examination of those years. We amended our tax returns for those years and reflected the impact of those amendments within current and deferred domestic income tax balance sheet accounts at each of the annual reporting dates through December 31, 2004.

Tax matters also includes the results of assessing the other restatement entries to determine which amounts had a corresponding impact on our provision for income taxes.

The following table presents the impact of the restatement adjustments, further described below, and of the business classified as discontinued operations in 2004 that is described in Note 3, on our consolidated statements of operations for the three and nine months ended September 30, 2003:

Consolidated Statements of Operations Information
For the Three and Nine Months Ended September 30, 2003

(Amounts in thousands, except per share data)	Three months ended September 30, 2003: As Previously Reported	Three months ended September 30, 2003: As Restated	Three months ended September 30, 2003: As Restated with Discontinued Operations	Nine months ended September 30, 2003: As Previously Reported	Nine months ended September 30, 2003: As Restated	Nine months ended September 30, 2003: As Restated with Discontinued Operations
Sales	$ 565,146	$ 561,777	$ 555,955	$1,743,193	$ 1,738,320	$ 1,721,324
Cost of sales	392,253	392,978	387,275	1,220,830	1,218,684	1,203,895
Gross profit	172,893	168,799	168,680	522,363	519,636	517,429
Selling, general and administrative expense	132,942	132,378	131,881	391,713	390,868	389,034
Integration expense	3,836	3,836	3,836	15,908	15,908	15,908
Restructuring expense	—	—	—	1,820	1,820	1,820
Operating income	36,115	32,585	32,963	112,922	111,040	110,667
Interest expense	(20,874)	(20,874)	(20,874)	(63,313)	(63,313)	(63,313)
Interest income	1,722	1,745	1,745	3,211	3,280	3,280
Loss on debt repayment and extinguishment	(369)	(369)	(369)	(1,008)	(1,008)	(1,008)
Other expense, net	(412)	(1,353)	(1,353)	(2,855)	(5,551)	(5,551)
Earnings before income taxes	16,182	11,734	12,112	48,957	44,448	44,075
Provision for income taxes	5,583	1,860	2,000	16,890	14,649	14,511
Income from continuing operations	10,599	9,874	10,112	32,067	29,799	29,564
Discontinued operations, net of tax	—	—	(238)	—	—	235
Net earnings	$ 10,599	$ 9,874	$ 9,874	$ 32,067	$ 29,799	$ 29,799
Net earnings per share — basic:						
Continuing operations	$ 0.19	$ 0.18	$ 0.18	$ 0.58	$ 0.54	$ 0.54
Discontinued operations	—	—	—	—	—	—
Net earnings	$ 0.19	$ 0.18	$ 0.18	$ 0.58	$ 0.54	$ 0.54
Net earnings per share — diluted:						
Continuing operations	$ 0.19	$ 0.18	$ 0.18	$ 0.58	$ 0.54	$ 0.54
Discontinued operations	—	—	—	—	—	—
Net earnings	$ 0.19	$ 0.18	$ 0.18	$ 0.58	$ 0.54	$ 0.54

Our restatement corrects the consolidated statements of operations for the following errors:

- Sales decreased $3.4 million and $4.9 million for the three and nine months ended September 30, 2003, respectively, primarily due to an error in the application of percentage of completion accounting for one long-term contract that includes subcontractors ($3.7 million for both the three and nine months ended September 30, 2003), and errors that reported sales in a period later than determined in accordance with GAAP for which there is no significant impact on net earnings in the periods presented ($0.5 million increase and $1.0 million decrease for the three and nine months ended September 30, 2003, respectively) and errors in other account reconciliations.
- Cost of sales increased for the three months ended September 30, 2003 and decreased for the nine months ended September 30, 2003, primarily due to errors in the following (in thousands):

	Three months	Nine months
Inventory valuation	$ 764	$ (1,505)
Pension expense	(388)	(1,164)
Intercompany reconciliations	239	1,803
Other (mainly errors in account reconciliations)	110	(1,280)
Total cost of sales	$ 725	$ (2,146)

- Selling, general and administrative expense decreased for the three and nine months ended September 30, 2003, primarily due to errors in the following (in thousands):

	Three months	Nine months
Long-term contract accounting	$ (876)	$ (876)
Pension expense	297	261
Fixed assets and intangibles	—	888
Other (mainly errors in account reconciliations)	15	(1,118)
Total selling, general and administrative expense	$ (564)	$ (845)

- Other expense, net increased $0.9 million and $2.7 million for the three and nine months ended September 30, 2003, respectively, primarily due to errors in the accounting for foreign currency forward contracts that did not meet the criteria for hedge accounting ($0.3 million and $1.5 million for the three and nine months ended September 30, 2003, respectively), unclaimed property ($0.3 million in each of the three and nine months ended September 30, 2003) and other individually insignificant errors.
- Provision for income taxes decreased $3.7 million and $2.2 million for the three and nine months ended September 30, 2003, respectively, primarily due to corrections in deferred tax accounts and the income tax effect of the errors described above. Included in this was $1.6 million for both the three and nine months ended September 30, 2003 due to the tax impact on the restatement items.

The following table presents the impact of the restatement adjustments on our consolidated statements of comprehensive income for the three and nine months ended September 30, 2003:

Consolidated Statements of Comprehensive Income Information
For the Three and Nine Months Ended September 30, 2003

	Three months ended September 30, 2003		Nine months ended September 30, 2003	
(Amounts in thousands)	As Previously Reported	As Restated	As Previously Reported	As Restated
Net earnings	$ 10,599	$ 9,874	$ 32,067	$ 29,799
Other comprehensive income (expense):				
Foreign currency translation adjustments, net of tax	(4,577)	(5,244)	27,483	32,655
Cash flow hedging activity, net of tax	1,429	1,081	164	687
Other comprehensive (loss) income	(3,148)	(4,163)	27,647	33,342
Comprehensive income	$ 7,451	$ 5,711	$ 59,714	$ 63,141

Our consolidated statement of cash flows for the nine months ended September 30, 2003, was also restated for the items discussed above. The following table presents the major subtotals in our 2003 consolidated statements of cash flows and the related impact of the restatement adjustments discussed above:

Condensed Consolidated Statements of Cash Flows Information
For the Nine Months Ended September 30, 2003

(Amounts in thousands)	Nine months ended September 30, 2003 As Previously Reported	Nine months ended September 30, 2003 As Restated
Net cash flows provided (used) by:		
Operating activities	$ 113,367	$ 115,530
Investing activities	(16,910)	(16,910)
Financing activities	(122,767)	(121,428)
Effect of exchange rate changes on cash	6,991	6,991
Net change in cash and cash equivalents	(19,319)	(15,817)
Cash and cash equivalents at beginning of year	49,293	48,991
Cash and cash equivalents at end of period	$ 29,974	$ 33,174

The footnotes contained in these condensed consolidated financial statements also reflect the impact of the restatement discussed in this footnote.

3. Discontinued Operations

In the first quarter of 2004, we made a definitive decision to sell our Government Marine Business Unit (“GMBU”), a business within our Flowserve Pump Division (“FPD”). As a result, we reclassified the operation to discontinued operations in the first quarter of 2004. In November 2004, we sold GMBU to Curtiss-Wright Electro-Mechanical Corporation for approximately $28 million, generating a pre-tax gain of $7.4 million after the allocation of approximately $8 million of FPD goodwill and $1 million of intangible assets. GMBU, which provided pump technology and service for U.S. Navy submarines and aircraft carriers, did not serve our core market and represented only a small part of our total pump business. We used net proceeds from the disposition of GMBU to reduce our outstanding indebtedness. As a result of this sale, we have presented the assets, liabilities and results of operations of the GMBU as discontinued operations for all periods included.

GMBU generated the following results of operations:

(Amounts in millions)	Three Months Ended September 30, 2004	2003 (As restated)
Sales	$ 7.4	$ 5.8
Cost of sales	6.0	5.7
Selling, general and administrative expense	0.7	0.5
Earnings (loss) before income taxes	0.7	(0.4)
Provision (benefit) for income taxes	0.2	(0.1)
Results for discontinued operations, net of tax	$ 0.5	$ (0.3)

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Sales	$ 19.1	$ 17.0
Cost of sales	15.3	14.8
Selling, general and administrative expense	2.3	1.8
Earnings before income taxes	1.5	0.4
Provision for income taxes	0.5	0.1
Results for discontinued operations, net of tax	$ 1.0	$ 0.3

GMBU's assets and liabilities have been reclassified to prepaid expenses and other, property, plant and equipment, net, accounts payable and accrued liabilities to reflect discontinued operations. As of September 30, 2004 and December 31, 2003, GMBU's assets and liabilities consisted of the following:

(Amounts in millions)	September 30, 2004	December 31, 2003
Accounts receivable, net	$ 3.3	$ 3.9
Inventory, net	6.4	5.7
Property, plant and equipment, net	1.3	1.6
Goodwill	7.8	7.8
Other intangible assets, net	1.4	1.4
Total assets	$ 20.2	$ 20.4
Accounts payable	$ 2.6	$ 3.3
Accrued liabilities	0.2	2.0
Total liabilities	$ 2.8	$ 5.3

4. Acquisition

We acquired the remaining 75% interest in Thompsons, Kelly and Lewis, Pty. Ltd ("TKL") an Australian manufacturer and supplier of pumps, during March 2004. The incremental interests acquired were accounted for as a step acquisition and TKL's results of operations have been consolidated since the date of acquisition. The estimated fair value of the net assets acquired (including approximately $2.2 million of cash acquired) exceeded the cash paid of $12 million and, accordingly, no goodwill was recognized.

5. Derivative Instruments and Hedges

We enter into forward contracts to hedge our risk associated with transactions denominated in currencies other than the local currency of the operation engaging in the transaction. Our risk management and derivatives policy specify the conditions in which we enter into derivative contracts. As of September 30, 2004, we have approximately $83.4 million of notional amount in outstanding contracts with third parties. As of September 30, 2004, the maximum length of any forward contract in place was 20 months.

Certain of our forward contracts do not qualify for hedge accounting. The fair value of these outstanding forward contracts at September 30, 2004 was an asset of $0.8 million and an asset of $4.7 million at December 31, 2003. Unrealized losses from the changes in the fair value of these forward contracts of $3,000 and $0.3 million for the quarters ended September 30, 2004 and 2003, respectively, and $4.6 million and $1.5 million for the nine months ended September 30, 2004 and 2003, respectively, are included in other expense, net in the consolidated statements of operations. The fair value of outstanding forward contracts qualifying for hedge accounting at September 30, 2004 was an asset of $0.1 million and a liability of $2.3 million at December 31, 2003. Unrealized gains (losses) from the changes in the fair value of qualifying forward contracts and the associated underlying exposures of $(49,000) and $144,000, net of tax, for the quarters ended September 30, 2004 and 2003, respectively, and $86,000 and $189,000, net of tax, for the nine months ended September 30, 2004 and 2003, respectively, are included in other comprehensive income (loss).

Also as part of our risk management program, we enter into interest rate swap agreements to hedge exposure to floating interest rates on certain portions of our debt. As of September 30, 2004, we have $125 million of notional amount in outstanding interest rate swaps with third parties. As of September 30, 2004, the maximum remaining length of any interest rate contract in place was approximately 26 months. The fair value of the interest rate swap agreements was a liability of $4.6 million and $7.6 million at September 30, 2004 and December 31, 2003, respectively. Unrealized gains from the changes in fair value of our interest rate swap agreements, net of reclassifications, of $2.1 million and $1.0 million, net of tax, for the quarters ended September 30, 2004 and 2003, respectively, and $1.8 million and $0.2 million, net of tax, for the nine months ended September 30, 2004 and 2003, respectively, are included in other comprehensive income (loss).

During the third quarter of 2004, we entered into a compound derivative contract to hedge exposure to both currency translation and interest rate risks associated with our European Investment Bank (“EIB”) loan. The notional amount of the derivative was $85 million, and it served to convert floating rate interest rate risk to a fixed rate, as well as U.S. dollar currency risk to Euros. The derivative matures in 2011. At September 31, 2004, the fair value of this derivative was a liability of $6.0 million. This derivative did not qualify for hedge accounting. The unrealized loss on the derivative, offset with the foreign currency translation gain on the underlying loan aggregates to $3.1 million for the three months ended September 30, 2004, and is included in other expense, net in the consolidated statements of operations.

We are exposed to risk from credit-related losses resulting from nonperformance by counterparties to our financial instruments. We perform credit evaluations of our counterparties under forward contracts and interest rate swap agreements and expect all counterparties to meet their obligations. We have not experienced credit losses from our counterparties. Additionally, we are exposed to risk of our derivative contracts not qualifying for hedge accounting.

6. Debt

Debt, including capital lease obligations, consisted of:

(Amounts in thousands)	September 30, 2004	December 31, 2003
Term Loan Tranche A:		
U.S. Dollar Tranches, interest rate of 4.47% in 2004 and 3.74% in 2003	**$ 138,524**	$ 200,004
Euro Tranche, interest rate of 4.62% in 2004 and 4.65% in 2003	**12,152**	12,292
Term Loan Tranche C, interest rate of 4.67% in 2004 and 4.00% in 2003	**374,473**	465,473
Senior Subordinated Notes, net of discount, coupon of 12.25%:		
U.S. Dollar denominated	**186,938**	186,739
Euro denominated	**80,162**	80,998
EIB loan, interest rate of 1.76% in 2004	**85,000**	—
Receivable factoring obligations	**4,189**	4,543
Capital lease obligations and other	**599**	752
Debt and capital lease obligations	**882,037**	950,801
Less amounts due within one year	**70,636**	71,035
Total debt due after one year	**$ 811,401**	$ 879,766

2000 Credit Facilities

As of September 30, 2004 and December 31, 2003, our 2000 Credit Facilities were composed of Tranche A and Tranche C term loans and a revolving line of credit. Tranche A consisted of a U.S. dollar denominated tranche and a Euro denominated tranche, the latter of which was a term note due in 2006. During the nine months ended September 30, 2004, we made scheduled, mandatory and optional debt payments of $27.5 million, $85.0 million and $40.0 million, respectively. During the remainder of 2004, we made mandatory and optional principal payments of $82.9 million and $120.0 million, respectively.

The Tranche A and Tranche C loans had ultimate maturities of June 2006 and June 2009, respectively. The term loans bore floating interest rates based on the London Interbank Offered Rate ("LIBOR") plus a borrowing spread, or the prime rate plus a borrowing spread, at our option. The borrowing spread for the senior credit facilities can increase or decrease based on the leverage ratio as defined in the credit facility and on our public debt ratings.

As part of the 2000 Credit Facilities, we also had a $300 million revolving line of credit that was set to expire in June 2006. The revolving line of credit allows us to issue up to $200 million in letters of credit. No amounts were outstanding under the revolving line of credit at September 30, 2004 or December 31, 2003. We had outstanding letters of credit of $48.2 million at September 30, 2004 under the revolving line of credit, which reduced borrowing capacity to $251.8 million, compared with a borrowing capacity of $257.3 million at December 31, 2003.

We were required, under certain circumstances as defined in the 2000 Credit Facilities, to use a percentage of excess cash generated from operations to reduce the outstanding principal of the term loans in the following year. Based upon the annual calculations performed at December 31, 2003, no additional principal payments became due in 2004 under this provision.

Senior Subordinated Notes

At September 30, 2004, we had $188.5 million and €65 million (equivalent to $80.8 million at September 30, 2004) face value of Senior Subordinated Notes outstanding. The Senior Subordinated Notes were originally issued in 2000 at a discount to yield 12.5%, but have a coupon interest rate of 12.25%. Interest on these notes was payable semi-annually in February and August. In August 2005, all remaining Senior Subordinated Notes outstanding were called by us at 106.125% of face value as specified in the loan agreement and repaid, along with accrued interest.

EIB Credit Facility

On April 14, 2004, we and one of our European subsidiaries, Flowserve B.V., entered into an agreement with EIB, pursuant to which EIB agreed to loan us up to €70 million, with the ability to draw funds in multiple currencies, to finance in part specified research and development projects undertaken by us in Europe. Borrowings under the EIB credit facility bear interest at a fixed or floating rate of interest agreed to by us and EIB with respect to each borrowing under the facility. Loans under the EIB credit facility are subject to mandatory repayment, at EIB's discretion, upon the occurrence of certain events, including a change of control or prepayment of certain other indebtedness. In addition, the EIB credit facility contains covenants that, among other things, limit our ability to dispose of assets related to the financed project and require us to deliver to EIB our audited annual financial statements within 30 days of publication. Our obligations under the EIB credit facility are guaranteed by a letter of credit outstanding under our New Credit Facilities.

In August 2004, we borrowed $85 million at a floating interest rate based on 3-month U.S. LIBOR that resets quarterly. As of September 30, 2004, the interest rate was 1.76%. The maturity of the amount drawn is June 15, 2011, but may be repaid at any time without penalty. Concurrent with borrowing the $85 million we entered into a derivative contract with a third party financial institution, swapped this principal amount to €70.6 million and fixed the LIBOR portion of the interest rate to a fixed interest rate of 4.19% through the scheduled repayment date. We have not applied hedge accounting to the derivative contract, and the unrealized loss on the derivative, offset with the foreign currency translation gain on the underlying loan aggregates to $3.1 million for the three months ended September 30, 2004, and is included in other expense, net in the consolidated statements of operations.

Accounts Receivable Securitization

In October 2004, one of our wholly owned subsidiaries entered into an accounts receivable securitization whereby we could obtain up to $75 million in financing by securitizing certain U.S.-based receivables with a third party. In October 2005, we terminated this accounts receivable securitization facility. In connection with the termination, we borrowed approximately $48 million under our New Credit Facilities to repurchase our receivables then held by such third party.

Debt Covenants

Our 2000 Credit Facilities that have now been refinanced, the letter of credit facility guaranteeing our obligations under the EIB credit facility, and the agreements governing our domestic receivables program each required us to deliver to creditors thereunder our audited annual consolidated financial statements within a specified number of days following the end of each fiscal year. In addition, the indentures governing our 12.25% Senior Subordinated Notes required us to timely file with the SEC our annual and quarterly reports.

7. Inventories

Inventories are stated at lower of cost or market. Cost is determined for principally all U.S. inventories by the LIFO method and for other inventories by the first-in, first-out ("FIFO") method.

Inventories and the method of determining costs were:

(Amounts in thousands)	**September 30, 2004**	December 31, 2003
Raw materials	**$ 127,818**	$ 115,695
Work in process	**216,252**	229,049
Finished goods	**246,511**	230,234
Less: Progress billings	**(81,759)**	(92,490)
Less: Excess and obsolete reserve	**(44,958)**	(43,354)
	463,864	439,134
LIFO reserve	**(27,768)**	(26,760)
Net inventory	**$ 436,096**	$ 412,374
Percent of inventory accounted for by:		
LIFO	**51%**	50%
FIFO	**49%**	50%

8. Restructuring Costs — IFC

Restructuring Costs

In conjunction with the acquisition of the Flow Control Division of Invensys plc ("IFC") during 2002, we initiated a restructuring program designed to reduce costs and eliminate excess capacity by closing 18 valve facilities, including 10 service facilities, and reducing sales and related support personnel. Our actions, some of which were approved and committed to in 2002 with the remaining actions approved and committed to in 2003, are expected to result in a gross reduction of approximately 889 positions and a net reduction of approximately 662 positions. Net position eliminations represent the gross positions eliminated from the closed facilities offset by positions added at the receiving facilities, which are required to produce the products transferred into the receiving facilities.

We established a restructuring program reserve upon acquisition of IFC, and recognized additional accruals of $4.5 million in 2003 for this program, including $3.2 million during the first nine months, primarily related to the closure of certain valve service facilities and the related reductions in workforce. Cash expenditures against the accrual were $11.6 million in 2003, including $9.5 million during the first nine months, and $2.7 million during the first nine months of 2004. The remaining accrual of $6.6 million reflects payments to be made in 2004 and beyond for severance obligations due to terminated personnel in Europe of $4.0 million as well as lease and other contract termination and exit costs of $2.6 million.

Cumulative costs associated with the closure of Flowserve facilities of $7.2 million through December 31, 2003, have been recognized as restructuring expense in operating results, whereas cumulative costs associated with the closure of IFC facilities of $17.9 million, including related deferred taxes of $6.2 million, became part of the purchase price allocation of the transaction. The effect of these closure costs increased the amount of goodwill otherwise recognizable as a result of the IFC acquisition.

The following illustrates activity related to the IFC restructuring reserve:

(Amounts in millions)	Severance	Other Exit Costs	Total
Balance at January 1, 2003	$ 10.7	$ 5.7	$ 16.4
Additional accruals	3.8	0.7	4.5
Cash expenditures	(8.8)	(2.8)	(11.6)
Balance at December 31, 2003	5.7	3.6	9.3
Cash expenditures	(0.9)	(0.4)	(1.3)
Balance at March 31, 2004	4.8	3.2	8.0
Cash expenditures	(0.4)	(0.3)	(0.7)
Balance at June 30, 2004	4.4	2.9	7.3
Cash expenditures	(0.4)	(0.3)	(0.7)
Balance at September 30, 2004	$ 4.0	$ 2.6	$ 6.6

Integration Costs – IFC

We did not incur acquisition-related integration expenses in 2004. During the three and nine months ended September 30, 2003, we incurred acquisition-related integration expense in conjunction with IFC, which is summarized below:

(Amounts in millions)	Three Months ended September 30, 2003	Nine Months ended September 30, 2003
Personnel and related costs	$ 1.0	$ 7.3
Transfer of product lines	0.7	4.1
Asset impairments	—	0.8
Other	2.1	3.7
IFC integration expense	$ 3.8	$ 15.9
Cash expense	$ 3.1	$ 14.3
Non-cash expense	0.7	1.6
IFC integration expense	$ 3.8	$ 15.9

The acquisition-related activities resulted in integration costs as categorized above and further defined as follows. Personnel and related costs include payroll, benefits, consulting fees, and retention and integration performance bonuses paid to our employees and contractors for the development, management and execution of the integration plan. Transfer of product lines includes costs associated with the transfer of product lines as well as realignment required in the receiving facilities. Asset impairments reflect the loss on disposal of property, plant and equipment at the facilities closed and disposal of inventory for discontinued product lines when the facilities were combined. The other category includes costs associated with information technology integration, legal entity consolidations, legal entity name changes, signage, new product literature and others. None of these items individually amounted to greater than $0.5 million.

Remaining Restructuring and Integration Costs – IFC

At December 31, 2003, we largely completed restructuring and integration activities related to IFC, except for payments to be made for certain European activities. We expect to incur no additional restructuring and integration costs related to this integration program. Payments from the restructuring accrual will continue throughout 2004 and into 2005 due to the timing of severance obligations in Europe.

9. Earnings Per Share

Basic and diluted earnings per weighted average share outstanding were calculated as follows:

	Quarter Ended September 30,	
(Amounts in thousands, except per share amounts)	2004	2003 (As restated)
Income from continuing operations	$ 5,955	$ 10,112
Net earnings	$ 6,368	$ 9,874
Denominator for basic earnings per share — weighted average shares	55,174	55,148
Effect of potentially dilutive securities	607	227
Denominator for diluted earnings per share — weighted average shares	55,781	55,375
Net earnings per share:		
Basic:		
Continuing operations	$ 0.11	$ 0.18
Net earnings	0.12	0.18
Diluted:		
Continuing operations	$ 0.10	$ 0.18
Net earnings	0.11	0.18

(Amounts in thousands, except per share amounts)	Nine Months Ended September 30, 2004	2003 (As restated)
Income from continuing operations	**$ 18,808**	$ 29,564
Net earnings	**$ 19,783**	$ 29,799
Denominator for basic earnings per share — weighted average shares	**54,976**	55,138
Effect of potentially dilutive securities	**552**	104
Denominator for diluted earnings per share — weighted average shares	**55,528**	55,242
Net earnings per share:		
Basic:		
Continuing operations	**$ 0.34**	$ 0.54
Net earnings	**0.36**	0.54
Diluted:		
Continuing operations	**$ 0.33**	$ 0.54
Net earnings	**0.35**	0.54

Options outstanding with an exercise price greater than the average market price of the common stock were not included in the computation of diluted earnings per share.

The following summarizes options to purchase common stock that were excluded from the computations of potentially dilutive securities:

	Quarter Ended September 30, 2004	2003
Total number excluded	**926,960**	1,240,679
Weighted average exercise price	**$ 27.40**	$ 27.12

	Nine Months Ended September 30, 2004	2003
Total number excluded	**1,040,346**	3,063,360
Weighted average exercise price	**$ 26.52**	$ 21.91

10. Legal Matters and Contingencies

We are a defendant in a large number of pending lawsuits (which include, in many cases, multiple claimants) that seek to recover damages for personal injury allegedly caused by exposure to asbestos containing products manufactured and/or distributed by us in the past. Any such products were encapsulated and used only as components of process equipment, and we do not believe that any emission of respirable asbestos fibers occurred during the use of this equipment. We believe that a high percentage of the applicable claims are covered by applicable insurance or indemnities from other companies.

On February 4, 2004, we received an informal inquiry from the SEC requesting the voluntary production of documents and information related to our February 3, 2004 announcement that we would restate our financial results for the nine months ended September 30, 2003 and the full years 2002, 2001 and 2000. On June 2, 2004, we were advised that the SEC had issued a formal order of private investigation into issues regarding this restatement and any other issues that arise from the investigation. We continue to cooperate with the SEC in this matter.

During the quarter ended September 30, 2003, related lawsuits were filed in federal court in the Northern District of Texas (the “Court’’), alleging that we violated federal securities laws. Since the filing of these cases, which have been consolidated, the lead plaintiff has amended its complaint several times. The lead plaintiff’s current pleading is the fifth consolidated amended complaint (“Complaint’’). The Complaint alleges that federal securities violations occurred between February 6, 2001 and September 27, 2002 and names as defendants Mr. C. Scott Greer, our former Chairman, President and Chief Executive Officer, Ms. Renee J. Hornbaker, our former Vice President and Chief Financial Officer, PricewaterhouseCoopers LLP, our independent registered public accounting firm, and Banc of America Securities LLC and Credit Suisse First Boston LLC, which served as underwriters for two of our public stock offerings during the relevant period. The Complaint asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, and Sections 11 and 15 of the Securities Act of 1933. The lead plaintiff seeks unspecified compensatory damages, forfeiture by Mr. Greer and Ms. Hornbaker of unspecified incentive-based or equity-based compensation and profits from any stock sales, and recovery of costs. On November 22, 2005, the Court entered an order denying the defendants' motions to dismiss the Complaint on the pleadings in their entirety. The case is currently set for trial on March 27, 2007. We continue to believe that the lawsuit is without merit and are vigorously defending the case.

We have been involved as a potentially responsible party ("PRP'') at former public waste disposal sites that may be subject to remediation under pending government procedures. The sites are in various stages of evaluation by federal and state environmental authorities. The projected cost of remediation at these sites, as well as our alleged "fair share'' allocation, is uncertain and speculative until all studies have been completed and the parties have either negotiated an amicable resolution or the matter has been judicially resolved. At each site, there are many other parties who have similarly been identified, and the identification and location of additional parties is continuing under applicable federal or state law. Many of the other parties identified are financially strong and solvent companies that appear able to pay their share of the remediation costs. Based on our information about the waste disposal practices at these sites and the environmental regulatory process in general, we believe that it is likely that ultimate remediation liability costs for each site will be apportioned among all liable parties, including site owners and waste transporters, according to the volumes and/or toxicity of the wastes shown to have been disposed of at the sites. We believe that our exposure for existing disposal sites will be less than $100,000.

We are also a defendant in several other lawsuits, including product liability claims, that are insured, subject to the applicable deductibles, arising in the ordinary course of business. Based on currently available information, we believe that we have adequately accrued estimated probable losses for such lawsuits. We are also involved in a substantial number of labor claims, including one case where we had a confidential settlement reflected in our results of operations for the second quarter of 2004.

Although none of the aforementioned potential liabilities can be quantified with absolute certainty, we have established reserves covering these exposures, which we believe to be reasonable based on past experience and available facts. While additional exposures beyond these reserves could exist, they currently cannot be estimated. We will continue to evaluate these potential contingent loss exposures and, if they develop, recognize expense as soon as such losses become probable and can be reasonably estimated.

We are also involved in ordinary routine litigation incidental to our business, none of which we believe to be material to our business, operations or overall financial condition. However, resolutions or dispositions of claims or lawsuits by settlement or otherwise could have a significant impact on our operating results for the reporting period in which any such resolution or disposition occurs.

11. Retirement and Postretirement Benefits

Components of the net periodic cost (benefit) for the three months ended September 30, 2004 and 2003 were as follows:

	U.S. Defined Benefit Plans		Non-U.S. Defined Benefit Plans		Postretirement Medical Benefits	
(Amounts in millions)	2004	2003	2004	2003	2004	2003
Net periodic cost (benefit)						
Service cost	$ 3.5	$ 3.4	$ 0.9	$ 0.6	$ 0.1	$ —
Interest cost	3.8	4.0	2.2	1.9	1.3	1.5
Expected return on plan assets	(4.3)	(4.3)	(1.1)	(0.9)	—	—
Curtailments/settlements	0.6	0.7	—	—	—	—
Amortization of unrecognized net loss	0.6	0.2	0.3	0.4	0.4	0.3
Amortization of prior service costs	(0.3)	(0.3)	—	—	(0.8)	(0.8)
Net cost recognized	$ 3.9	$ 3.7	$ 2.3	$ 2.0	$ 1.0	$ 1.0

Components of the net periodic cost (benefit) for the nine months ended September 30, 2004 and 2003 were as follows:

(Amounts in millions)	U.S. Defined Benefit Plans 2004	U.S. Defined Benefit Plans 2003	Non-U.S. Defined Benefit Plans 2004	Non-U.S. Defined Benefit Plans 2003	Postretirement Medical Benefits 2004	Postretirement Medical Benefits 2003
Net periodic cost (benefit)						
Service cost	$ 10.4	$ 10.1	$ 2.5	$ 1.9	$ 0.1	$ 0.2
Interest cost	11.6	11.9	6.6	5.8	4.0	4.4
Expected return on plan assets	(13.0)	(12.9)	(3.3)	(2.8)	—	—
Curtailments/settlements	0.6	0.5	—	0.1	—	—
Amortization of unrecognized net loss	1.9	0.6	1.0	1.0	1.1	1.0
Amortization of prior service costs	(1.0)	(1.0)	—	—	(2.3)	(2.5)
Net cost recognized	$ 10.5	$ 9.2	$ 6.8	$ 6.0	$ 2.9	$ 3.1

12. Income taxes

For the three months ended September 30, 2004, we earned $15.9 million before taxes and provided for income taxes of $9.9 million, resulting in an effective tax rate of 62.5%. For the nine months ended September 30, 2004, we earned $52.5 million before taxes and provided for income taxes of $33.7 million, resulting in an effective tax rate of 64.2%. The effective tax rate varied from the U.S. federal statutory rate for the three and nine months ended September 30, 2004 primarily due to the impact of increased foreign earnings repatriation used to pay down U.S. debt.

13. Segment Information

We are principally engaged in the worldwide design, manufacture, distribution and service of industrial flow management equipment. We provide pumps, valves and mechanical seals primarily for the petroleum industry, chemical-processing industry, power-generation industry, water industry, general industry and other industries requiring flow management products.

We have the following three divisions, each of which constitutes a business segment:

- Flowserve Pump Division;
- Flow Control Division; and
- Flow Solutions Division.

Each division manufactures different products and is defined by the type of products and services provided. Each division has a President, who reports directly to our Chief Executive Officer, and a Division Controller, who reports directly to our Chief Accounting Officer. For decision-making purposes, our Chief Executive Officer and other members of senior executive management use financial information generated and reported at the division level. Our corporate headquarters does not constitute a separate division or business segment.

We evaluate segment performance and allocate resources based on each segment’s operating income excluding special items, such as restructuring and integration costs related to the IFC acquisition. We believe that special items, while indicative of efforts to integrate acquired companies such as IFC and IDP into our business, do not reflect ongoing business results. We believe investors and other users of our financial statements can better evaluate and analyze historical and future business trends if special items are excluded from each segment’s operating income. Operating income before special items is not a recognized measure under GAAP and should not be viewed as an alternative to, or a better indicator of, GAAP measures of performance.

Amounts classified as All Other include the corporate headquarters costs and other minor entities that do not constitute separate segments. Intersegment sales and transfers are recorded at cost plus a profit margin, with the margin on such sales eliminated with consolidation.

Effective January 1, 2004, we realigned certain small sites between segments. Accordingly, the segment information for all periods presented herein has been reported under our revised organizational structure.

The following is a summary of the financial information of the reportable segments reconciled to the amounts reported in the condensed consolidated financial statements.

Three Months Ended September 30, 2004 (amounts in thousands)	**Flowserve Pump**	**Flow Solutions**	**Flow Control**	**Subtotal – Reportable Segments**	**All Other**	**Consolidated Total**
Sales to external customers	**$ 322,468**	**$ 88,749**	**$ 239,479**	**$ 650,696**	**$ 1,438**	**$ 652,134**
Intersegment sales	**1,362**	**7,143**	**1,052**	**9,557**	**(9,557)**	**—**
Segment operating income	**23,482**	**18,761**	**17,020**	**59,263**	**(17,837)**	**41,426**

Three Months Ended September 30, 2003 (As restated) (amounts in thousands)	**Flowserve Pump**	**Flow Solutions**	**Flow Control**	**Subtotal – Reportable Segments**	**All Other**	**Consolidated Total**
Sales to external customers	$256,730	$ 84,059	$ 213,367	$ 554,156	$ 1,799	$ 555,955
Intersegment sales	1,148	5,211	966	7,325	(7,325)	—
Segment operating income (before special items) (1)	16,225	17,129	11,329	44,683	(7,884)	36,799

(1) Special items reflect costs associated with the IFC acquisition including $3.8 million of integration expense and $0 of restructuring expense.

A reconciliation of total consolidated operating income before special items to consolidated earnings before income taxes follows:

(amounts in thousands)	Three Months Ended September 30, **2004**	2003 (As restated)
Total consolidated operating income (before special items)	**$ 41,426**	$ 36,799
Less:		
Net interest expense	**(20,492)**	(19,129)
Loss on optional prepayments of debt	**(963)**	(369)
Other expense, net	**(4,107)**	(1,353)
Special items:		
Integration expense	**—**	3,836
Earnings before income taxes	**$ 15,864**	$ 12,112

Nine Months Ended September 30, 2004 (amounts in thousands)	Flowserve Pump	Flow Solutions	Flow Control	Subtotal – Reportable Segments	All Other	Consolidated Total
Sales to external customers	**$ 935,615**	**$ 266,309**	**$ 699,647**	**$ 1,901,571**	**$ 4,189**	**$ 1,905,760**
Intersegment sales	**4,328**	**22,297**	**3,405**	**30,030**	**(30,030)**	**—**
Segment operating income	**64,620**	**54,524**	**50,337**	**169,481**	**(47,255)**	**122,226**

Nine Months Ended September 30, 2003 (As restated) (amounts in thousands)	Flowserve Pump	Flow Solutions	Flow Control	Subtotal – Reportable Segments	All Other	Consolidated Total
Sales to external customers	$821,890	$247,623	$647,432	$1,716,945	$ 4,379	$1,721,324
Intersegment sales	4,274	17,141	5,102	26,517	(26,517)	—
Segment operating income (before special items) (1)	57,831	50,242	44,548	152,621	(24,226)	128,395

(1) Special items reflect costs associated with the IFC acquisition including $15.9 million of integration expense and $1.8 million of restructuring expense.

A reconciliation of total consolidated operating income before special items to consolidated earnings before income taxes follows:

	Nine Months Ended September 30, 2004	Nine Months Ended September 30, 2003 (As restated)
(amounts in thousands)		
Total consolidated operating income (before special items)	**$ 122,226**	$ 128,395
Less:		
Net interest expense	**(59,758)**	(60,033)
Loss on optional prepayments of debt	**(1,048)**	(1,008)
Other expense, net	**(8,916)**	(5,551)
Special items:		
Integration expense	**—**	15,908
Restructuring expense	**—**	1,820
Earnings before income taxes	**$ 52,504**	$ 44,075

14. Subsequent Events

Financing Matters

In March 2005 we obtained consents from our major lenders that enhanced our flexibility under our 2000 Credit Facilities to among other things permit the August 2005 refinancing of our 2000 Credit Facilities and the repurchase of our 12.25% Senior Subordinated Notes. On August 12, 2005, we entered into New Credit Facilities comprised of a $600 million term loan expiring on August 10, 2012 and a $400 million revolving line of credit, which can be utilized to provide up to $300 million in letters of credit, expiring on August 12, 2010. We refer to these credit facilities collectively as our New Credit Facilities. The proceeds of borrowings under our New Credit Facilities were used to call our 12.25% Senior Subordinated Notes and retire our indebtedness outstanding under our 2000 Credit Facilities. We also replaced the letter of credit agreement guaranteeing our obligations under the EIB credit facility described in Note 6 with a letter of credit issued under the new revolving line of credit.

We incurred $9.3 million in fees related to the new facilities, of which $0.3 million were expensed in 2005. Prior to the refinancing, we had $11.8 million of unamortized deferred loan costs related to the 2000 Credit Facilities and the Senior Subordinated Notes. Based upon the final syndicate of financial institutions for the New Credit Facilities, we expensed $10.5 million of these unamortized deferred loan costs in 2005. In addition to the total loan costs of $10.8 million that were expensed, we recorded a charge of $16.5 million for premiums paid to call the Senior Subordinated Notes, for a total loss on extinguishment of $27.3 million recorded in 2005. The remaining $9.0 million of fees related to the new facilities were capitalized and combined with the remaining $1.3 million of previously unamortized deferred loan costs for a total of $10.3 million in deferred loan costs included in other assets, net. These costs will be amortized over the term of the New Credit Facilities.

Borrowings under our New Credit Facilities bear interest at a rate equal to, at our option, either (1) the base rate (which is based on greater of the prime rate most recently announced by the administrative agent under our New Credit Facilities or the Federal Funds rate plus 0.50%) or (2) LIBOR plus an applicable margin determined by reference to the ratio of our total debt to consolidated Earnings before Interest, Taxes, Depreciation and Amortization ("EBITDA"), which at December 31, 2005 was 1.75% for LIBOR borrowings. In addition, we pay lenders under the New Credit Facilities a commitment fee equal to a percentage, determined by reference to the ratio of our total debt to consolidated EBITDA, of the unutilized portion of the revolving line of credit, and letter of credit fees with respect to each financial standby letter of credit outstanding under our New Credit Facilities equal to a percentage based on the applicable margin in effect for LIBOR borrowings under the new revolving line of credit. The fee for performance standby letters of credit is 0.5% lower than the fee for financial standby letters of credit.

In connection with the New Credit Facilities, during 2005 we entered into $275 million of notional amount of interest rate swaps to hedge exposure of floating interest rates. Of this total notional amount of $275 million, $130 million carried a start date of September 30, 2005 and $145 million carried a start date of December 30, 2005. These swaps, combined with the $135 million of interest rates swaps held by us at the time of the refinancing, total $410 million of notional amount of interest rate swaps outstanding at December 31, 2005.

Our obligations under the New Credit Facilities are unconditionally guaranteed, jointly and severally, by substantially all of our existing and subsequently acquired or organized domestic subsidiaries. In addition, prior to our obtaining and maintaining investment grade credit ratings, our and the guarantors' obligations under the New Credit Facilities are collateralized by substantially all of our and the guarantors' assets.

The loans under our New Credit Facilities are subject to mandatory repayment with, in general:

- 100% of the net cash proceeds of asset sales; and
- Unless we attain and maintain investment grade credit ratings:
  - 75% of our excess cash flow, subject to a reduction based on the ratio of our total debt to consolidated EBITDA;
  - 50% of the proceeds of any equity offerings; and
  - 100% of the proceeds of any debt issuances (subject to certain exceptions).

We may prepay loans under our New Credit Facilities in whole or in part, without premium or penalty.

As a result of the 2004 Restatement and the new obligations regarding internal controls attestation under Section 404, we did not timely issue our financial statements for the year ended December 31, 2004 and the quarterly periods ended June 30, 2004, September 30, 2004, March 31, 2005, June 30, 2005 and September 30, 2005, and were unable to timely file with the SEC our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q for such periods. Prior to the refinancing of our 2000 Credit Facilities and the replacement of the standby letter of credit facility, we obtained waivers thereunder extending the deadline for the delivery of our financial statements to the lenders under our 2000 Credit Facilities and the letter of credit facility guaranteeing the EIB credit facility and, as a result of such waivers, were not in default. We did not seek or obtain a waiver under the indentures governing our 12.25% Senior Subordinated Notes with respect to our inability to timely file with the SEC the required reports and, prior to the refinancing of our 12.25% Senior Subordinated Notes, were in default thereunder. However, our debt is properly classified as non-current in our balance sheet as we demonstrated our ability and intent to obtain new long-term credit facilities in August 2005.

We have determined, utilizing our restated financial information, that on multiple occasions we did not comply with some of the financial covenants in our 2000 Credit Facilities, which are no longer in effect. We believe that we could have undertaken readily available actions to maintain compliance or obtained a waiver or amendment to the 2000 Credit Facilities had the new restated results then been known. We have complied with all other non-financial covenants under our 2000 Credit Facilities. We believe that these covenant violations have no impact on our New Credit Facilities and that the amounts outstanding under the 2000 Credit Facilities are properly classified in our consolidated balance sheet.

Our New Credit Facilities contain covenants requiring us to deliver to lenders leverage and interest coverage financial covenants and our audited annual and unaudited quarterly financial statements. Under the leverage covenant, the maximum permitted leverage ratio steps down beginning with the fourth quarter of 2006, with a further step-down beginning with the fourth quarter of 2007. Under the interest coverage covenant, the minimum required interest coverage ratio steps up beginning with the fourth quarter of 2006, with a further step-up beginning with the fourth quarter of 2007. Compliance with these financial covenants under our New Credit Facilities is tested quarterly, and we have complied with the financial covenants as of December 31, 2005. Delivery of the December 31, 2004 audited consolidated financial statements was required by December 31, 2005 and delivery of the December 31, 2005 audited financial statements is required by May 30, 2006. We received a waiver from our lenders to deliver the December 31, 2004 audited financial statements by February 28, 2006. The December 31, 2004 audited financial statements were delivered February 13, 2006. Further, we are required to furnish to our lenders within 50 days of the end of each of the first three quarters of each year our consolidated balance sheet, and related statements of operations, shareholders' equity and cash flows.

Our New Credit Facilities also contain covenants restricting our and our subsidiaries' ability to dispose of assets, merge, pay dividends, repurchase or redeem capital stock and indebtedness, incur indebtedness and guarantees, create liens, enter into agreements with negative pledge clauses, make certain investments or acquisitions, enter into sale and leaseback transactions, enter into transactions with affiliates, make capital expenditures, engage in any business activity other than our existing business or any business activities reasonably incidental thereto. With the waiver for delivery of the December 31, 2004 audited financial statements, we are currently in compliance with all debt covenants under the New Credit Facilities.

Legal Matters

On October 6, 2005, a shareholder derivative lawsuit was filed purportedly on our behalf in the 193rd Judicial District of Dallas County, Texas. The lawsuit names as defendants Mr. Greer, Ms. Hornbaker, and current board members Hugh K. Coble, George T. Haymaker, Jr., William C. Rusnack, Michael F. Johnston, Charles M. Rampacek, Kevin E. Sheehan, Diane C. Harris, James O. Rollans and Christopher A. Bartlett. We are named as a nominal defendant. Based primarily on the purported misstatements alleged in the above-described federal securities case, the plaintiff asserts claims against the defendants for breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets and unjust enrichment. The plaintiff alleges that these purported violations of state law occurred between April 2000 and the date of suit. The plaintiff seeks on our behalf an unspecified amount of damages, injunctive relief and/or the imposition of a constructive trust on defendants' assets, disgorgement of compensation, profits or other benefits received by the defendants from us, and recovery of attorneys' fees and costs. We strongly believe that the suit was improperly filed and have filed a motion seeking dismissal of the case.

On February 7, 2006, we received a subpoena from the SEC regarding goods and services that we delivered to Iraq from 1996 through 2003 during the United Nations Oil-for-Food Program. We are in the process of reviewing and responding to the subpoena and intend to cooperate with the SEC. We believe that other companies in our industry (as well as in other industries) have received similar subpoenas and requests for information.

On March 14, 2006, a shareholder derivative lawsuit was filed purportedly on our behalf in federal court in the Northern District of Texas. The lawsuit names as defendants Mr. Greer, Ms. Hornbaker, and current board members Hugh K. Coble, George T. Haymaker, Jr., Lewis M. Kling, William C. Rusnack, Michael F. Johnston, Charles M. Rampacek, Kevin E. Sheehan, Diane C. Harris, James O. Rollans and Christopher A. Bartlett. We are named as a nominal defendant. Based primarily on certain of the purported misstatements alleged in the above-described federal securities case, the plaintiff asserts claims against the defendants for breaches of fiduciary duty. The plaintiff alleges that the purported breaches of fiduciary duty occurred between 2000 and 2004. The plaintiff seeks on our behalf an unspecified amount of damages, disgorgement by Mr. Greer and Ms. Hornbaker of salaries, bonuses, restricted stock and stock options, and recovery of attorneys' fees and costs. We strongly believe that the suit was improperly filed and intend to file a motion seeking dismissal of the case.

Since we manufacture and sell our products globally, we are subject to risks associated with doing business internationally. In March 2006, we initiated a process to determine our compliance posture with respect to U.S. export control laws and regulations. Upon initial investigation, it appears that some product transactions and technology transfers require further research to determine compliance with U.S. export control laws and regulations. With assistance from outside counsel, we are currently involved in a systematic process to conduct further research. Any potential violations of U.S. export control laws and regulations that are identified may result in civil or criminal penalties, including fines and/or suspension of the privilege to engage in export transactions or to have our foreign affiliates receive U.S.-origin goods, software or technology. Because our research into this issue is ongoing, we are unable to determine the extent of any violations or the nature or amount of any potential penalties to which we might be subject to in the future. As a result, we cannot currently predict whether the resolution of this matter will materially adversely affect our financial position or results of operations. At this time, we have not made any provision in our consolidated financial statements for any fines or penalties that might be incurred relating to this matter.

Stock Matters

On June 1, 2005, we took action to extend to December 31, 2006, the regular term of certain options granted to employees, including executive officers, qualified retirees and directors, which were scheduled to expire in 2005. Subsequently, we took action on November 4, 2005, to extend the exercise date of these options, and options expiring in 2006, to January 1, 2009. We thereafter concluded, however, that recent regulatory guidance issued under Section 409A of the Internal Revenue Code might cause the recipients' extended options to become subject to unintended adverse tax consequences under Section 409A. Accordingly, effective December 14, 2005, the Organization and Compensation Committee of the Board of Directors partially rescinded, in accordance with the regulations, the extensions of the regular term of these options, to provide as follows:

(i) the regular term of options otherwise expiring in 2005 will expire 30 days after the options first become exercisable when our SEC filings have become current and an effective SEC Form S-8 Registration Statement has been filed with the SEC, and

(ii) the regular term of options otherwise expiring in 2006 will expire on the later of:

  (1) 75 days after the regular term of the option as originally granted expires, or

  (2) December 31, 2006 (assuming the options become exercisable in 2006 for the reasons included in (i) above).

These extensions are subject to our shareholders approving certain applicable plan amendments at our next annual shareholders' meeting, scheduled for August 2006. If shareholders do not approve the plan amendments as currently posed in our proxy statement, these extension actions will become void. If such plan amendments are approved at our next annual shareholders' meeting, the extensions will be considered as a stock modification for financial reporting purposes subject to the recognition of a non-cash compensation charge in accordance with SFAS No. 123(R), "Share-Based Payment". Our actual charge will be contingent upon many factors, including future share price volatility, risk free interest rate, option maturity, strike price, share price and dividend yield.

The earlier extension actions also extended the option exercise period available following separation from employment for reasons of death, disability and termination not for cause or certain voluntary separations. These separate extensions were partially rescinded at the December 14, 2005, meeting of the Organization and Compensation Committee of the Board of Directors, and as so revised are currently effective and not subject to shareholder approval. The exercise period available following such employment separations has been extended to the later of (i) 30 days after the options first became exercisable when our SEC filings have become current and an effective SEC Form S-8 Registration Statement has been filed with the SEC, or (ii) the period available for exercise following separation from employment under the terms of the option as originally granted. This extension is considered for financial reporting purposes as a stock modification subject to the recognition of a non-cash compensation change in accordance with APB No. 25, "Accounting for Stock Issued to Employees," of approximately $1 million in 2005. The extension of the exercise period following separation from employment does not apply to option exercise periods governed by a separate separation contract or agreement.

Other Matters

In the first quarter of 2005, we made a definitive decision to sell certain non-core service operations, collectively called the General Services Group ("GSG") and engaged an investment banking firm to commence marketing. As a result, we reclassified the operation to discontinued operations in the first quarter of 2005. Sales for GSG were $116 million in 2004. Total assets at December 31, 2004 ascribed to GSG were approximately $63 million. We performed an impairment analysis of long-lived assets on a held and used basis, and concluded that no impairment was warranted as of December 31, 2004. GSG was sold on December 31, 2005 for approximately $16 million in gross cash proceeds, subject to final working capital adjustments, while retaining approximately $12 million of net accounts receivable. We used approximately $11 million of the net cash proceeds to reduce our indebtedness. In 2005, we recorded an impairment loss of approximately $31 million related to GSG.

To promote continuity of senior management, in March 2005 our Board of Directors approved a Transitional Executive Security Plan, which provides cash and stock-based incentives to key management personnel to remain employed by us for the near term. As a result of this plan, we recorded additional compensation expenses in 2005 of approximately $3 million. See "Transitional Executive Security Plan" in Item 11 of our 2004 Annual Report for a detailed discussion on this plan.

During 2005, we made a number of modifications to our stock plans, including the acceleration of certain restricted stock grants and outstanding options, as well as the extension of the exercise period associated with certain outstanding options. These modifications resulted from severance agreements with former executives and from our decision to temporarily suspend option exercises. As a result of the modifications, we recorded additional compensation expenses in 2005 of approximately $7 million based upon the intrinsic values of the awards, primarily related to severance agreements with former executives, on the dates the modifications were made.

As a result of the severance and executive search payments related to the management changes of approximately $2 million, expenses under the Transitional Executive Security Plan described above and stock compensation expense resulting from the modification of our stock option plans described above, we recorded total incremental compensation expense of approximately $12 million in 2005.

We have recently concluded an IRS audit of our U.S. federal income tax returns for the years 1999 through 2001. Based on its audit work, the IRS has issued proposed adjustments to increase taxable income during 1999 through 2001 by $12.8 million, and to deny foreign tax credits of $2.9 million in the aggregate. The tax liability resulting from these proposed adjustments will be offset with foreign tax credit carryovers and other refund claims, and therefore should not result in a material future cash payment, pending final review by the Joint Committee on Taxation. The effect of the adjustments to current and deferred taxes has been reflected in the consolidated financial statements for annual periods covered by the 2004 Restatement.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis should be read in conjunction with the information contained in the condensed consolidated financial statements and notes thereto included in this Quarterly Report and our 2004 Annual Report.

OVERVIEW

We produce engineered and industrial pumps, industrial valves, control valves, nuclear valves, valve actuation and precision mechanical seals, and provide a range of related flow management services worldwide, primarily for the process industries. Equipment manufactured and serviced by us is predominately used in industries that deal with difficult-to-handle and corrosive fluids as well as environments with extreme temperature, pressure, horsepower and speed. Our businesses are affected by economic conditions in the U.S. and other countries where our products are sold and serviced, by the cyclical nature of the petroleum, chemical, power, water and other industries served, by the relationship of the U.S. dollar to other currencies, and by the demand for and pricing of customers' products. We believe the impact of these conditions is somewhat mitigated by the strength and diversity of our product lines, geographic coverage and significant installed base, which provides potential for an annuity stream of revenue from parts and services.

RECENT DEVELOPMENTS

Restatement

This Quarterly Report includes our restated condensed consolidated financial statements for the three and nine months ended September 30, 2003 resulting from our 2004 Restatement.

The 2004 Restatement corrects errors made in the application of GAAP, including errors with respect to inventory valuation, long-term contract accounting, intercompany accounts, pension expense, fixed assets and intangibles, financial derivatives, unclaimed property, tax matters, and other adjustments from unreconciled accounts. The 2004 Restatement is more fully described in Note 2 to our condensed consolidated financial statements included in this Quarterly Report.

The impact of the 2004 Restatement decreased sales for the three and nine months ended September 30, 2003 by $3.4 million and $4.9 million, respectively, decreased net earnings for the three and nine months ended September 30, 2003 by $0.7 million and $2.3 million, respectively. Diluted net earnings per share decreased by $0.01 and $0.04 per share for the three and nine months ended September 30, 2003, respectively.

For further discussion of recent developments, see Note 14 to our condensed consolidated financial statements included in this Quarterly Report and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" included in our 2004 Annual Report.

RESULTS OF OPERATIONS — Three and Nine Months ended September 30, 2004 and 2003

Consolidated Results

Bookings, Sales and Backlog

	Quarter Ended September 30,	
(Amounts in millions)	**2004**	2003
		(As restated)
Bookings	**$ 664.7**	$ 581.0
Sales	**652.1**	556.0
Backlog	**896.6**	834.4

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Bookings	**$ 1,997.7**	$ 1,811.4
Sales	**1,905.8**	1,721.3
Backlog	**896.6**	834.4

We define a booking as the receipt of a customer order that contractually engages us to perform activities on behalf of our customer with regard to manufacture, service or support. Bookings for the three months ended September 30, 2004 increased by $61.5 million, or 10.6%, excluding currency benefits of approximately $22 million, as compared with the same period in 2003. Bookings for the nine months ended September 30, 2004 increased by $99.4 million, or 5.5%, excluding currency benefits of approximately $87 million, as compared with the same period in 2003. The increases are primarily attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $15.5 million and $29.2 million for the three and nine months ended September 30, 2004, respectively, and is included in our Flowserve Pump Division, and strengthening markets in the oil and gas industry, as well as the North American and European regions.

Sales for the three months ended September 30, 2004 increased by $73.5 million, or 13.2%, excluding currency benefits of approximately $23 million, as compared with the same period in 2003. Sales for the nine months ended September 30, 2004 increased by $101.6 million, or 5.9%, excluding currency benefits of approximately $83 million, as compared with the same period in 2003. The increases are primarily attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $11.0 million and $25.1 million for the three and nine months ended September 30, 2004, respectively, and is included in our Flowserve Pump Division, and strengthening markets in the oil and gas industry, as well as the North American and European regions.

Net sales to international customers, including export sales from the U.S., were 63% of sales in the third quarter of 2004 compared with 60% in the same period in 2003, and 63% of sales in the first nine months of 2004 as compared with 57% in the same period in 2003. Favorable currency translation was the primary factor for the increase in 2004 compared with the prior period.

Backlog represents the accumulation of uncompleted customer orders. Backlog at September 30, 2004 increased by $35.8 million, or 4.3%, excluding currency benefits of approximately $26 million, as compared with September 30, 2003. The backlog increase compared with the prior year resulted from increased bookings during the third quarter of 2004.

Gross Profit and Gross Profit Margin

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Gross profit	**$ 193.8**	$ 168.7
Gross profit margin	**29.7%**	30.3%

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Gross profit	**$ 570.4**	$ 517.4
Gross profit margin	**29.9%**	30.1%

Gross profit margin of 29.7% for the three months ending September 30, 2004 decreased from 30.3% for the same period in 2003, primarily due to increased price competition and warranty costs experienced by our Flowserve Pump Division. Gross profit margin of 29.9% for the nine months ending September 30, 2004 was relatively flat with the same period in 2003.

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

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
SG&A expense	**$ 152.4**	$ 131.9
SG&A expense as a percentage of sales	**23.4%**	23.7%

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
SG&A expense	**$ 448.2**	$ 389.0
SG&A expense as a percentage of sales	**23.5%**	22.6%

SG&A for the three months ended September 30, 2004 increased by $16.5 million, or 12.5%, excluding currency effects of approximately $4 million, as compared with the same period in 2003. The increase in SG&A is due primarily to higher professional fees of $7.7 million generally related to the restatement and legal matters, as well as higher incentive compensation accruals of $7.8 million.

SG&A for the nine months ended September 30, 2004 increased by $43.1 million, or 11.1%, excluding currency effects of approximately $16 million, as compared with the same period in 2003. The increase in SG&A is due primarily to higher professional fees of $23.8 million generally related to the restatement and legal matters, as well as higher incentive compensation accruals of $12.1 million.

Integration and Restructuring Expense

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Integration expense	**$ —**	$ 3.8
Restructuring expense	**—**	—

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Integration expense	**$ —**	$ 15.9
Restructuring expense	**—**	1.8

There were no integration or restructuring expenses in 2004 due to the substantial completion of the program at the end of 2003. The integration and restructuring expenses in 2003 relate to the integration of IFC into the Flow Control Division. Integration expense represents period costs associated with IFC acquisition-related reorganizations such as relocation of product lines from closed to receiving facilities, realignment of receiving facilities, performance and retention bonuses, idle manufacturing costs, costs related to the integration team and asset impairments. Restructuring expense represents severance and other exit costs related to our valve facility closures and reductions in work force. We have largely completed our restructuring and integration activities related to IFC, except for completion of certain European integration activities. See the discussion on "Restructuring and Acquisition Related Charges" included in this Management's Discussion and Analysis for a more detailed description of the integration and restructuring program.

Operating Income

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Operating income	**$ 41.4**	$ 33.0
Operating income as a percentage of sales	**6.3%**	5.9%

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Operating income	**$ 122.2**	$ 110.7
Operating income as a percentage of sales	**6.4%**	6.4%

Operating income for the three months ended September 30, 2004 increased by $5.7 million, or 17.4%, excluding currency benefits of approximately $3 million, as compared with the same period in 2003. The increase is primarily a result of the decrease of $3.8 million in integration and restructuring expenses in 2004, as well as improved cost controls that resulted in decreased administrative costs by our divisions. These are partially offset by the increase in SG&A discussed above.

Operating income for the nine months ended September 30, 2004 increased by $2.6 million, or 2.4%, excluding currency benefits of approximately $9 million, as compared with the same period in 2003. The increase is primarily a result of the decrease of $17.7 million in integration and restructuring expenses in 2004 partially offset by the increase in SG&A discussed above.

Interest Expense, Interest Income and Loss on Repayment of Debt

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Interest expense	**$ 21.2**	$ 20.9
Interest income	**0.7**	1.7
Loss on optional prepayments of debt	**1.0**	0.4

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Interest expense	**$ 61.0**	$ 63.3
Interest income	**1.2**	3.3
Loss on optional prepayments of debt	**1.0**	1.0

Interest expense for the three months ended September 30, 2004 increased by $0.3 million as compared with the same period in 2003, primarily due to increased interest rates in 2004. Interest expense for the nine months ended September 30, 2004 decreased by $2.3 million, as compared with the same period in 2003 primarily due to reduced debt levels associated with optional and scheduled debt paydowns since September 30, 2003. Approximately 54% of our debt was at fixed rates at September 30, 2004, including the effects of $125 million notional interest rate swaps.

Interest income was lower than the first quarter of 2003 due to a lower average cash balance in 2004.

During both the three and nine months ended September 30, 2004, we recognized expenses of $1.0 million, for the write-off of unamortized prepaid financing fees related to optional debt repayments of $40.0 million. For the same periods in 2003, we incurred expenses of $0.4 million and $1.0 million, respectively, related to optional debt prepayments.

Other Expense, net

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Other expense, net	**$ (4.1)**	$ (1.4)

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Other expense, net	**$ (8.9)**	$ (5.6)

Other expense, net for the three months ended September 30, 2004 increased by $2.7 million as compared with the same period in 2003 primarily due to increases in foreign currency transaction losses, partially offset by unrealized gains on forward contracts that did not qualify for hedge accounting.

Other expense, net for the nine months ended September 30, 2004 increased by $3.3 million as compared with the same period in 2003 due to increases in unrealized losses on forward contracts that did not qualify for hedge accounting and increases in foreign currency transaction losses.

Tax Expense and Tax Rate

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Provision for income tax	**$ 9.9**	$ 2.0
Effective tax rate	**62.5%**	16.5%

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Provision for income tax	**$ 33.7**	$ 14.5
Effective tax rate	**64.2%**	32.9%

Our effective tax rate of 62.5% for the three months ended September 30, 2004 increased from 16.5% for the same period in 2003. Our effective tax rate of 64.2% for the nine months ended September 30, 2004 increased from 32.9% for the same period in 2003. The increases are due to increased foreign earnings repatriation in 2004 used to pay down U.S. debt. We utilized prior year foreign tax credit carry forwards against the tax liability resulting from these repatriations. However, the benefit of a significant portion of these foreign tax credit carry forwards was recognized in prior years' effective tax rates. Also, our effective tax rate was significantly lower in 2003 resulting from the recognition of a significant U.S. tax refund received in the third quarter of 2003.

Net Earnings and Earnings Per Share

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Income from continuing operations	**$ 6.0**	$ 10.1
Net earnings	**6.4**	9.9
Net earnings per share from continuing operations — diluted	**0.10**	0.18
Net earnings per share — diluted	**0.11**	0.18
Average diluted shares	**55.7**	55.4

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Income from continuing operations	**$ 18.8**	$ 29.6
Net earnings	**19.8**	29.8
Net earnings per share from continuing operations — diluted	**0.33**	0.54
Net earnings per share — diluted	**0.35**	0.54
Average diluted shares	**55.5**	55.2

Net earnings for the three months ended September 30, 2004 decreased by $3.5 million, or 35.4%, as compared with the same period in 2003, and net earnings per share decreased $0.06 over the same period. The decrease in net earnings reflects the increases in SG&A and tax expense discussed above, which are partially offset by the decrease in integration and restructuring expenses.

Net earnings for the nine months ended September 30, 2004 decreased by $10.0 million, or 33.6%, as compared with the same period in 2003, and net earnings per share decreased $0.18 over the same period. The decrease in net earnings reflects the increases in SG&A and tax expense discussed above, which are partially offset by the decrease in integration and restructuring expenses, as well as the decrease in interest expense.

Average diluted shares were relatively flat in the first nine months of 2004 compared with the same period in 2003.

Other Comprehensive Income (Loss)

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Other comprehensive income (loss)	**$ (1.5)**	$ (4.2)

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Other comprehensive income (loss)	**$ (15.4)**	$ 33.3

Other comprehensive income (loss) for the three months ended September 30, 2004 increased $2.7 million as compared with the same period in 2003, reflecting an increase in unrealized hedging losses, partially offset by a strengthening of the Euro during the three-month period ended September 30, 2004, as compared with a slight weakening of the Euro during the same period in 2003.

Other comprehensive income (loss) for the nine months ended September 30, 2004 decreased $48.7 million as compared with the same period in 2003, reflecting a weakening of the Euro during the nine-month period ended September 30, 2004, as compared with a strengthening of the Euro during the same period in 2003, as well as an increase in unrealized hedging losses.

Business Segments

We conduct our business through three business segments that represent our major product areas: 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 related services; and Flow Solutions Division (“FSD”) for precision mechanical seals and related services. We evaluate segment performance and allocate resources based on each segment’s operating income excluding special items, such as restructuring and integration costs related to the IFC acquisition. We believe that special items, while indicative of efforts to integrate IFC in our business, do not reflect ongoing business results. We believe investors and other users of our financial statements can better evaluate and analyze historical and future business trends if special items are excluded from each segment’s operating income. Operating income before special items is not a recognized measure under GAAP and should not be viewed as an alternative to, or a better indicator of, GAAP measures of performance. Effective January 1, 2004, we realigned certain small sites between segments. Accordingly, the segment information for all periods presented herein has been reported under our revised organizational structure. See Note 13 to our condensed consolidated financial statements included in this Quarterly Report for further discussion of our segments. The key operating results for our three business segments, FPD, FCD and FSD are discussed below.

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 has 27 manufacturing facilities worldwide, of which nine are located in North America, 10 in Europe, and eight in South America and Asia. FPD also has 65 service centers, which are either free standing or co-located in a manufacturing facility.

	Quarter Ended September 30,	
(Amounts in millions)	**2004**	2003
		(As restated)
Bookings	**$ 349.7**	$ 281.5
Sales	**323.8**	257.9
Gross profit	**82.9**	67.4
Gross profit margin	**25.6%**	26.1%
Operating income	**23.5**	16.2
Operating income as a percentage of sales	**7.3%**	6.3%
Backlog	**628.3**	584.8

	Nine Months Ended September 30,	
(Amounts in millions)	**2004**	2003
		(As restated)
Bookings	**$ 1,011.1**	$ 904.7
Sales	**939.9**	826.2
Gross profit	**235.7**	204.8
Gross profit margin	**25.1%**	24.8%
Operating income	**64.6**	57.8
Operating income as a percentage of sales	**6.9%**	7.0%
Backlog	**628.3**	584.8

Bookings for the three months ended September 30, 2004 increased by $56.3 million, or 20.0%, excluding currency benefits of approximately $12 million, as compared with the same period in 2003. The increase is primarily attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $15.5 million, and the strength of the oil and gas industry due to sustained high crude oil prices, which contributed to increased bookings in both North America and Europe.

Bookings for the nine months ended September 30, 2004 increased by $63.1 million, or 7.0%, excluding currency benefits of approximately $43 million, as compared with the same period in 2003. The increase is primarily attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $29.2 million, and improvements in the oil and gas industry.

Sales for the three months ended September 30, 2004 increased by $54.6 million, or 21.2%, excluding currency benefits of approximately $11 million, as compared with the same period in 2003. The increase is attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $11.0 million, and an increase in aftermarket sales in Europe.

Sales for the nine months ended September 30, 2004 increased by $72.0 million, or 8.7%, excluding currency benefits of approximately $42 million, as compared with the same period in 2003. The increase is attributable to our acquisition of the remaining 75% of TKL in March 2004, which contributed $25.1 million, and improvements in the oil and gas industry.

Gross profit margin of 25.6% for the three months ending September 30, 2004 decreased from 26.1% for the same period in 2003. The decrease is due to increased price competition and warranty costs, partially offset by an increase in higher margin aftermarket sales. Gross profit margin of 25.1% for the nine months ending September 30, 2004 increased slightly from 24.8% for the same period in 2003.

Operating income for the three months ended September 30, 2004 increased by $6.0 million, or 37.2%, excluding currency benefits of approximately $1 million, as compared with the same period in 2003. The increase is due to improvements in administrative cost controls and improved collection of past due accounts, as well as a contribution of $0.8 million due to our acquisition of the remaining 75% of TKL. These improvements are partially offset by an increase in incentive compensation of $2.3 million and an increase in professional fees of $1.2 million.

Operating income for the nine months ended September 30, 2004 increased by $2.9 million, or 5.0%, excluding currency benefits of approximately $4 million, as compared with the same period in 2003. The increase is due primarily to our acquisition of the remaining 75% of TKL in March 2004, which contributed $1.8 million, and the slight increase in gross profit margin. These benefits are partially offset by an increase in incentive compensation of $4.2 million and an increase in professional fees, primarily legal, of $5.9 million.

Flow Control Division

Through FCD, we design, manufacture and distribute industrial valves, manual valves, control valves, nuclear valves, actuators and related equipment, and provide a variety of flow control-related services. We manufacture valves and actuators through five major manufacturing plants in the U.S. and 17 major manufacturing plants outside the U.S. We have 51 valve service centers, of which 34 are related to GSG, that are generally free standing and principally based in the U.S. As a result of our 2002 acquisition of IFC, we believe we are one of the world’s leading suppliers of valves and related products and services to the chemical industry. Based on independent industry sources, we believe that we are the second largest industrial valve supplier on a global basis. We believe that our comprehensive portfolio of valve products and services is a key source of our competitive advantage. Further, our focus on service and severe corrosion and erosion applications is a key competency.

	Quarter Ended September 30,	
(Amounts in millions)	**2004**	2003
		(As restated)
Bookings	**$ 228.9**	$ 216.5
Sales	**240.5**	214.3
Gross profit	**69.5**	62.4
Gross profit margin	**28.9%**	29.1%
Operating income (before special items)	**17.0**	11.3
Integration expense	**—**	3.8
Operating income (after special items)	**17.0**	7.5
Operating income (before special items) as a percentage of sales	**7.1%**	5.3%
Backlog	**234.6**	215.9

	Nine Months Ended September 30,	
(Amounts in millions)	**2004**	2003
		(As restated)
Bookings	**$ 725.6**	$ 662.2
Sales	**703.1**	652.5
Gross profit	**209.0**	195.4
Gross profit margin	**29.7%**	29.9%
Operating income (before special items)	**50.3**	44.5
Integration expense	**—**	15.9
Restructuring expense	**—**	1.8
Operating income (after special items)	**50.3**	26.8
Operating income (before special items) as a percentage of sales	**7.2%**	6.8%
Backlog	**234.6**	215.9

Bookings for the three months ended September 30, 2004 increased by $3.8 million, or 1.7%, excluding currency benefits of approximately $9 million, as compared with the same period in 2003. The increase is due to $10.2 million in increased bookings related to control and process valves out of North America and a $1.0 million increase in Europe, the Middle East and Africa ("EMA"), primarily related to process valves in the United Kingdom. The bookings decreased by $5.2 million in Asia Pacific and by $2.3 million in the industrial services group. The decreases in Asia Pacific relate to decreases in Australia and Singapore, where control and process valves saw weakness in many end markets.

Bookings for the nine months ended September 30, 2004 increased by $28.4 million, or 4.3%, excluding currency benefits of approximately $35 million, as compared with the same period in 2003. The increase is due to the strengthening of markets in North America and EMA. The North American increase of $24.4 million reflects strengthening in many customer markets in process and control valves, with the increase in EMA of $20.4 million attributable to strong project bookings in the United Kingdom, Sweden and Germany across all customer markets. These increases were partially offset by $7.9 million of lower bookings for the industrial services group and by smaller decreases in bookings for Asia Pacific, primarily related to Australia.

Sales for the three months ended September 30, 2004 increased by $16.7 million, or 7.8%, excluding currency benefits of approximately $10 million, as compared with the same period in 2003. The increase is predominantly attributable to an $11.8 million increase in North America and a $3.4 million increase in Asia Pacific. The North American results reflect increased project business across all customer markets, whereas the Asia Pacific results primarily reflect the improvement in the project business for controls valves and, to a lesser extent, the power market.

Sales for the nine months ended September 30, 2004 increased by $17.8 million, or 2.7%, excluding currency benefits of approximately $33 million, as compared with the same period in 2003. The increase is attributable to North American sales increases of $17.1 million particularly for project sales in many customer markets and to increased project sales of $6.7 million in Asia Pacific primarily reflective of improved Singapore sales levels in the controls sector. These increases were partially offset by lower sales by our industrial services group, reflective of softness in the service business.

Gross profit margin of 28.9% and 29.7% for the three and nine months ending September 30, 2004, respectively, were relatively flat as compared with the same periods in 2003.

Operating income (before special items) for the three months ended September 30, 2004 increased by $4.5 million, or 39.8%, excluding currency benefits of approximately $1 million, as compared with the same period in 2003. This increase in operating income is predominantly attributable to approximately $4.0 million of higher gross profit primarily generated from the increased North American and Asia Pacific sales. Also, operating income was favorably impacted by $0.8 million in lower employee benefit costs and $0.8 million in lower advertising costs, which were offset by $2.1 million in higher incentive compensation.

Operating income (before special items) for the nine months ended September 30, 2004 increased by $2.3 million, or 5.1%, excluding currency benefits of approximately $4 million, as compared with the same period in 2003. The increase is attributable to approximately $3.0 million of higher gross profit, absent currency increases, associated with the aforementioned sales increases and decreases in employee benefit costs. Partially offsetting these positive effects are a $3.9 million increase in incentive compensation and a $1.2 million increase in professional fees. Special items during 2003 are associated with the acquisition and integration of IFC into FCD.

Flow Solutions Division

Through FSD, we design, manufacture and distribute mechanical seals, sealing systems and parts and provide related services, principally to industrial markets. FSD has seven manufacturing operations, four of which are located in North America, two are in Europe and one is in Singapore. FSD operates 62 QRCs worldwide, including 24 such sites in North America, 14 in Europe, and the remainder located in South America and Asia. Our ability to turn around engineered seal products within 72 hours from the customer's request, through design, engineering, manufacturing, testing and delivery, is our major source of competitive advantage. Based on independent industry sources, we believe that we are the second largest mechanical seal supplier on a global basis.

(Amounts in millions)	Quarter Ended September 30, 2004	2003 (As restated)
Bookings	**$ 98.5**	$ 88.7
Sales	**95.9**	89.3
Gross profit	**42.2**	38.0
Gross profit margin	**44.0%**	42.5%
Operating income	**18.8**	17.1
Operating income as a percentage of sales	**19.6%**	19.2%
Backlog	**46.6**	40.9

(Amounts in millions)	Nine Months Ended September 30, 2004	2003 (As restated)
Bookings	**$ 294.0**	$ 269.3
Sales	**288.6**	264.8
Gross profit	**126.3**	115.8
Gross profit margin	**43.8%**	43.7%
Operating income	**54.5**	50.2
Operating income as a percentage of sales	**18.9%**	19.0%
Backlog	**46.6**	40.9

Bookings for the three months ended September 30, 2004 increased by $8.1 million, or 9.1%, excluding currency benefits of approximately $2 million, as compared with the same period in 2003. Bookings for the nine months ended September 30, 2004 increased by $16.2 million, or 6.0%, excluding currency benefits of approximately $9 million, as compared with the same period in 2003. The bookings improvement generally reflects FSD's emphasis on end user business and success in establishing longer-term customer alliance programs. Increased market conditions and a focus on customer service also contributed to the increase.

Sales for the three months ended September 30, 2004 increased by $4.8 million, or 5.4%, excluding currency benefits of approximately $2 million, as compared with the same period in 2003. Sales for the nine months ended September 30, 2004 increased by $15.5 million, or 5.8%, excluding currency benefits of approximately $8 million, as compared with the same period in 2003. As discussed above, the improved market conditions, combined with heightened levels of service and customer alliance programs have contributed to the sales growth.

Gross profit margin of 44.0% for the three months ending September 30, 2004 increased from 42.5% for the same period in 2003. The increases are primarily attributable to increases in plant efficiencies and cost savings resulting from our Continuous Improvement Process ("CIP") initiative, and are partially offset by increases in worldwide metals prices. Gross profit margin of 43.8% for the nine months ending September 30, 2004 was flat as compared to the same period in 2003.

Operating income for the three months ended September 30, 2004 increased by $1.3 million, or 7.8%, as compared with the same period in 2003. Currency had a negligible impact on operating income for the quarter. Operating income for the nine months ended September 30, 2004 increased by $2.7 million, or 5.3%, excluding currency benefits of approximately $2 million, as compared with the same period in 2003. These improvements reflect the benefits of increased sales, as well as the operating efficiencies resulting from our CIP initiative.

RESTRUCTURING AND ACQUISITION RELATED CHARGES

Restructuring Costs

In conjunction with the IFC acquisition during 2002, we initiated a restructuring program designed to reduce costs and eliminate excess capacity by closing 18 valve facilities, including 10 service facilities, and reducing sales and related support personnel. Our actions, some of which were approved and committed to in 2002 with the remaining actions approved and committed to in 2003, are expected to result in a gross reduction of approximately 889 positions and a net reduction of

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approximately 662 positions. Net position eliminations represent the gross positions eliminated from the closed facilities offset by positions added at the receiving facilities, which are required to produce the products transferred into the receiving facilities.

We established a restructuring program reserve upon acquisition of IFC, and recognized additional accruals of $4.5 million in 2003 for this program, including $3.2 million during the first nine months, primarily related to the closure of certain valve service facilities and the related reductions in workforce. Cash expenditures against the accrual were $11.6 million in 2003, including $9.5 million during the first nine months, and $2.7 million during the first nine months of 2004. The remaining accrual of $6.6 million reflects payments to be made in 2004 and beyond for severance obligations due to terminated personnel in Europe of $4.0 million as well as lease and other contract termination and exit costs of $2.6 million.

Cumulative costs associated with the closure of Flowserve facilities of $7.2 million through December 31, 2003, have been recognized as restructuring expense in operating results, whereas cumulative costs associated with the closure of IFC facilities of $17.9 million, including related deferred taxes of $6.2 million, became part of the purchase price allocation of the transaction. The effect of these closure costs increased the amount of goodwill otherwise recognizable as a result of the IFC acquisition.

The following illustrates activity related to the IFC restructuring reserve:

(Amounts in millions)	Severance	Other Exit Costs	Total
Balance at January 1, 2003	$ 10.7	$ 5.7	$ 16.4
Additional accruals	3.8	0.7	4.5
Cash expenditures	(8.8)	(2.8)	(11.6)
Balance at December 31, 2003	5.7	3.6	9.3
Cash expenditures	(0.9)	(0.4)	(1.3)
Balance at March 31, 2004	4.8	3.2	8.0
Cash expenditures	(0.4)	(0.3)	(0.7)
Balance at June 30, 2004	4.4	2.9	7.3
Cash expenditures	(0.4)	(0.3)	(0.7)
Balance at September 30, 2004	$ 4.0	$ 2.6	$ 6.6

Remaining Restructuring and Integration Costs — IFC

We did not incur acquisition-related integration expenses in 2004 as, by December 31, 2003, we had largely completed restructuring and integration activities related to IFC, except for payments to be made for certain European activities. We expect to incur no additional restructuring and integration costs. Payments from the restructuring accrual will continue throughout 2004 and into 2005 due to the timing of severance obligations in Europe. For discussion of integration costs incurred in 2003 as a result of our acquisition of IFC, see Note 8 to the accompanying condensed consolidated financial statements included in this Quarterly Report.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Analysis

	Nine Months Ended September 30,	
(Amounts in millions)	**2004**	2003 (As restated)
Net cash flows provided by operating activities	**$ 86.8**	$ 115.5
Net cash flows used by investing activities	**(33.9)**	(16.9)
Net cash flows used by financing activities	**(66.0)**	(121.4)

Cash generated by operations and borrowings available under our existing revolving credit facility are our primary sources of short-term liquidity. Our sources of operating cash include the sale of our products and services. Our cash balance at September 30, 2004 was $40.5 million, as compared with $53.5 million at December 31, 2003.

Cash flows provided by operating activities in the first nine months of 2004 were $86.8 million, compared with $115.5 million in the first nine months of 2003. Working capital, excluding cash, was a source of operating cash flow of $3.8 million in the first nine months of 2004, compared with a source of $57.3 million in the prior year period. The reduction in working capital for the current period primarily reflects an increase of $18.7 million and $7.6 million in accrued liabilities and accounts payable, respectively, versus the prior year, partially offset by an increase in inventories of $20.9 million. The increase in accrued liabilities is due primarily to an increase in the accrual for annual incentive compensation, and the increase in accounts payable is primarily due to an increase in income taxes payable. The increase in inventory was generally due to the higher backlog.

Accounts receivable for the first nine months generated $4.1 million of cash flow compared with generation of $67.3 million of cash flow in the prior year, however, days' sales outstanding improved to 69 days from 72 days at September 30, 2003 due to the higher sales level. Inventory was a $20.9 million use of cash flow for the first nine months of 2004, compared with a $14.1 million source of cash in the prior year. Inventory turns improved to 4.2 times at September 30, 2004 compared with 3.8 times at September 30, 2003.

We made the following quarterly contributions to our U.S. defined benefit pension plans:

Quarter ending:	**2004**	2003
	(Amounts in millions)	
March 31	**$ 0.2**	$ 0.1
June 30	**8.1**	2.9
September 30	**5.3**	23.9
December 31	**1.7**	0.1
	$ 15.3	$ 27.0

Cash flows used by investing activities in the first nine months of 2004 were $33.9 million, compared with $16.9 million in the first nine months of 2003. Cash outflows in 2004 were primarily due to capital expenditures, as well as the acquisition of TKL in March 2004 (described below). Cash outflows in 2003 were due primarily to capital expenditures.

Cash flows used by financing activities in the first nine months of 2004 were $66.0 million, compared with $121.4 million in the first nine months of 2003. Cash outflows in both periods were primarily due to net payments of long-term debt.

We believe cash flows from operating activities combined with availability under our existing revolving credit agreement and our existing cash balance will be sufficient to enable us to meet our cash flow needs for the next 12 months. Cash flows from operations could be adversely affected by economic, political and other risks associated with sales of our products, operational factors, competition, fluctuations in foreign exchange rates and fluctuations in interest rates, among other factors.

Acquisitions

We regularly evaluate acquisition opportunities of various sizes. The cost and terms of any financing to be raised in conjunction with any acquisition, including our ability to raise economical capital, is a critical consideration in any such evaluation.

In March 2004, we acquired the remaining 75% interest in TKL for approximately $12 million. We paid for the acquisition with cash generated by operations. Prior to the acquisition, we held a 25% interest in TKL. As a result of this acquisition, we strengthened our product offering in the mining industry, broadened our manufacturing capacity in the Asia Pacific region and gained foundry capacity.

Capital Expenditures

Capital expenditures were $28.5 million for the nine months ended September 30, 2004, including approximately $5 million in July 2004 for the purchase of a building we previously leased for the manufacture of valves, compared with $19.1 million for the same period in 2003. Capital expenditures were funded primarily by operating cash flows. For each period, capital expenditures were invested in new and replacement machinery and equipment, information technology and acquisition integration activities, including structures and equipment required at receiving facilities. For the full year 2004, our capital expenditures were approximately $45 million. Certain of our facilities may face capacity constraints in the foreseeable future, which may lead to higher capital expenditure levels.

We received cash on disposal of a divestiture of a small distribution business of $3.6 million in the first quarter of 2004.

Financing

2000 Credit Facilities

On August 8, 2000, we entered into senior credit facilities comprised of a $275.0 million Tranche A term loan, a $475.0 million Tranche B term loan and a $300.0 million revolving line of credit, hereinafter collectively referred to as our “2000 Credit Facilities.” In connection with our acquisition of IFC in May 2002, we amended and restated our 2000 Credit Facilities to provide for (1) an incremental $95.3 million Tranche A term loan and (2) a $700.0 million Tranche C term loan. The proceeds of the incremental Tranche A term loan and the Tranche C term loan were used to finance a portion of the acquisition purchase price and to repay in full the Tranche B term loan.

Borrowings under our 2000 Credit Facilities bore interest at a rate equal to, at our option, either (1) the base rate (which was based on the prime rate most recently announced by the administrative agent under our 2000 Credit Facilities or the Federal Funds rate plus 0.50%) or (2) London Interbank Offered Rate (“LIBOR”), plus, in the case of Tranche A term loan and loans under the revolving line of credit, an applicable margin determined by reference to the ratio of our total debt to consolidated EBITDA, and, in the case of Tranche C term loan, an applicable margin based on our long-term debt ratings.

During the nine months ended September 30, 2004, we made scheduled, mandatory and optional debt payments of $27.5 million, $85.0 million and $40.0 million, respectively. During the remainder of 2004, we made mandatory and optional principal payments of $82.9 million and $120.0 million, respectively.

Senior Subordinated Notes

At September 30, 2004, we had $188.5 million and €65 million (equivalent to $80.8 million at September 30, 2004) face value of Senior Subordinated Notes outstanding. The Senior Subordinated Notes were originally issued in 2000 at a discount to yield 12.5%, but have a coupon interest rate of 12.25%. Interest on these notes was payable semi-annually in February and August. In August 2005, all remaining Senior Subordinated Notes outstanding were called by us at 106.125% of face value as specified in the loan agreement and repaid, along with accrued interest.

New Credit Facilities

On August 12, 2005, we entered into New Credit Facilities comprised of a $600.0 million term loan maturing on August 10, 2012 and a $400.0 million revolving line of credit, which can be utilized to provide up to $300.0 million in letters of credit, expiring on August 12, 2010. We used the proceeds of borrowings under our New Credit Facilities to refinance our 12.25% Senior Subordinated Notes and indebtedness outstanding under our 2000 Credit Facilities. Further, we replaced the letter of credit agreement that guaranteed our EIB credit facility (described below) with a letter of credit issued as part of the New Credit Facilities.

Borrowings under our New Credit Facilities bear interest at a rate equal to, at our option, either (1) the base rate (which is based on greater of the prime rate most recently announced by the administrative agent under our New Credit Facilities or the Federal Funds rate plus 0.50%) or (2) LIBOR plus an applicable margin determined by reference to the ratio of our total debt to consolidated EBITDA, which as of December 31, 2005 was 1.75% for LIBOR borrowings.

The loans under our New Credit Facilities are subject to mandatory repayment with, in general:

- 100% of the net cash proceeds of asset sales; and

- Unless we attain and maintain investment grade credit ratings:
  - 75% of our excess cash flow, subject to a reduction based on the ratio of our total debt to consolidated EBITDA;
  - 50% of the proceeds of any equity offerings; and
  - 100% of the proceeds of any debt issuances (subject to certain exceptions).

We may prepay loans under our New Credit Facilities in whole or in part, without premium or penalty.

EIB Credit Facility

On April 14, 2004, we and one of our European subsidiaries, Flowserve B.V., entered into an agreement with EIB, pursuant to which EIB agreed to loan us up to €70 million, with the ability to draw funds in multiple currencies, to finance in part specified research and development projects undertaken by us in Europe. Borrowings under the EIB credit facility bear interest at a fixed or floating rate of interest agreed to by us and EIB with respect to each borrowing under the facility. Loans under the EIB credit facility are subject to mandatory repayment, at EIB's discretion, upon the occurrence of certain events, including a change of control or prepayment of certain other indebtedness. In addition, the EIB credit facility contains covenants that, among other things, limit our ability to dispose of assets related to the financed project and require us to deliver to EIB our audited annual financial statements within 30 days of publication. Our obligations under the EIB credit facility are guaranteed by a letter of credit outstanding under our New Credit Facilities.

In August 2004 we borrowed $85 million at a floating interest rate based on 3-month U.S. LIBOR that resets quarterly. As of December 31, 2004, the interest rate was 2.39%. The maturity of the amount drawn is June 15, 2011, but may be repaid at any time without penalty. Concurrent with borrowing the $85 million we entered into a derivative contract with a third party financial institution, swapped this principal amount to €70.6 million and fixed the LIBOR portion of the interest rate to a fixed interest rate of 4.19% through the scheduled repayment date. We have not applied hedge accounting to the derivative contract, and the unrealized loss on the derivative, offset with the foreign currency translation gain on the underlying loan aggregates to $3.1 million for the three months ended September 30, 2004, and is included in other expense, net in the consolidated statements of operations.

Additional discussion of our 2000 Credit Facilities, New Credit Facilities, and EIB credit facility is included in Note 6 to our condensed consolidated financial statements, included in this Quarterly Report.

We have entered into interest rate and currency swap agreements to hedge our exposure to cash flows related to the credit facilities discussed above. These agreements are more fully described in "Item 3. Quantitative and Qualitative Disclosures about Market Risk."

Accounts Receivable Securitization

In October 2004, one of our wholly owned subsidiaries entered into an accounts receivable securitization whereby we could obtain up to $75 million in financing by securitizing certain U.S.-based receivables with a third party. In October 2005, we terminated this accounts receivable securitization facility. In connection with the termination, we borrowed approximately $48 million under our New Credit Facilities to repurchase our receivables then held by such third party.

Accounts Receivable Factoring

Through our European subsidiaries, we engage in non-recourse factoring of certain accounts receivable. The various agreements have different terms, including options for renewal and mutual termination clauses. Under our 2000 Credit Facilities, such factoring was generally limited to $50 million, based on due date of the factored receivables. The limit on factoring was raised to $75 million under the New Credit Facilities entered into in August 2005. See additional discussion of our accounts receivable factoring program in Note 6 to our consolidated financial statements included in our 2004 Annual Report.

Debt Covenants and Other Matters

Our 2000 Credit Facilities that have now been refinanced, the letter of credit facility guaranteeing our obligations under the EIB credit facility, and the agreements governing our domestic receivables program each required us to deliver to creditors thereunder our audited annual consolidated financial statements within a specified number of days following the end of each fiscal year. In addition, the indentures governing our 12.25% Senior Subordinated Notes required us to timely file with the SEC our annual and quarterly reports. As a result of the 2004 Restatement and the new obligations regarding internal controls attestation under Section 404, we did not timely issue our financial statements for the year ended December 31, 2004 and the quarterly periods ended June 30, 2004, September 30, 2004, March 31, 2005, June 30, 2005 and September 30, 2005, and were unable to timely file with the SEC our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q for such periods. Prior to the refinancing of our 2000 Credit Facilities and the replacement of the standby letter of credit facility, we obtained waivers thereunder extending the deadline for the delivery of our financial statements to the lenders under our 2000 Credit Facilities and the letter of credit facility guaranteeing the EIB credit facility and, as a result of such waivers, were not in default due to the delay in the delivery of our financial statements. We did not seek or obtain a waiver under the indentures governing our 12.25% Senior Subordinated Notes with respect to our inability to timely file with the SEC the required reports and, prior to the refinancing of our 12.25% Senior Subordinated Notes, were in default thereunder. However, our debt is properly classified as non-current in our balance sheet as we demonstrated our ability and intent to obtain new long-term credit facilities in August 2005.

We have determined, utilizing our restated financial information, that on multiple occasions we did not comply with some of the financial covenants in our 2000 Credit Facilities, which are no longer in effect. We believe that we could have undertaken readily available actions to maintain compliance or obtained a waiver or amendment to the 2000 Credit Facilities had the new restated results then been known. We have complied with all other non-financial covenants under our 2000 Credit Facilities. We believe that these covenant violations have no impact on our New Credit Facilities and that the amounts outstanding under the 2000 Credit Facilities are properly classified in our consolidated balance sheet.

Our New Credit Facilities contain covenants requiring us to deliver to lenders leverage and interest coverage financial covenants and our audited annual and unaudited quarterly financial statements. Under the leverage covenant, the maximum permitted leverage ratio steps down beginning with the fourth quarter of 2006, with a further step-down beginning with the fourth quarter of 2007. Under the interest coverage covenant, the minimum required interest coverage ratio steps up beginning with the fourth quarter of 2006, with a further step-up beginning with the fourth quarter of 2007. Compliance with these financial covenants under our New Credit Facilities is tested quarterly, and we have complied with the financial covenants as of December 31, 2005. Delivery of the December 31, 2005 audited financial statements is required by May 30, 2006. Further, we are required to furnish within 50 days of the end of each of the first three quarters of each year our consolidated balance sheet, and related statements of operations, shareholders’ equity and cash flows.

Our New Credit Facilities also contain covenants restricting our and our subsidiaries’ ability to dispose of assets, merge, pay dividends, repurchase or redeem capital stock and indebtedness, incur indebtedness and guarantees, create liens, enter into agreements with negative pledge clauses, make certain investments or acquisitions, enter into sale and leaseback transactions, enter into transactions with affiliates, make capital expenditures, engage in any business activity other than our existing business or any business activities reasonably incidental thereto. With the waiver for delivery of the December 31, 2004 audited financial statements, we are currently in compliance with all debt covenants under the New Credit Facilities.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management’s discussion and analysis are based on our condensed consolidated financial statements and related footnotes contained within this report. Our more critical accounting policies used in the preparation of the consolidated financial statements were discussed in our Annual Report on Form 10-K for the year ended December 31, 2004. These critical policies, for which no significant changes have occurred in the nine months ended September 30, 2004, include:

- Revenue Recognition;
- Accounts Receivable and Related Allowance for Doubtful Accounts;
- Inventories and Related Reserves;
- Deferred Tax Asset Valuation;
- Tax Reserves;
- Restructuring and Integration Expense;

- Legal and Environmental Accruals;
- Warranty Accruals;
- Pension and Postretirement Benefits Obligations; and
- Valuation of Goodwill, Indefinite-Lived Intangible Assets and Other Long-Lived Assets.

Based on an assessment of our accounting policies and the underlying judgments and uncertainties affecting the application of those policies, we believe that our condensed consolidated financial statements provide a meaningful and fair perspective of our financial position and results of operations. This is not to suggest that other general risk factors, such as changes in worldwide demand, changes in material costs, performance of acquired businesses and others, could not adversely impact our consolidated financial position, results of operations and cash flows in future periods.

The process of preparing financial statements in conformity with GAAP requires the use of estimates and assumptions to determine certain of the assets, liabilities, revenues and expenses. These estimates and assumptions are based upon the best information available at the time of the estimates or assumptions. The estimates and assumptions could change materially as conditions within and beyond our control change. Accordingly, actual results could differ materially from those estimates. The significant estimates are reviewed quarterly with our Audit/Finance Committee.

ACCOUNTING DEVELOPMENTS

We have presented the information about accounting pronouncements not yet implemented in Note 1 to our condensed consolidated financial statements included in this Quarterly Report.

Forward-Looking Information is Subject to Risk and Uncertainty

This Quarterly Report and other written reports and oral statements we make from time-to-time contain various “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995 and include assumptions about our future financial and market conditions, operations and results. In some cases forward looking statements can be identified by terms such as “may,” “will,” “should,” “expect,” “plans,” “seeks,” “anticipate,” “believe,” “estimate,” “predicts,” “potential,” “continue,” “intends,” or other comparable terminology. These statements are not historical facts or guarantees of future performance but instead are based on current expectations and are subject to significant risks, uncertainties and other factors, many of which are outside of our control. Among the many factors that could cause actual results to differ materially from the forward-looking statements are:

- we have material weaknesses in our internal control over financial reporting;
- continuing delays in our filing of our periodic public reports and any SEC, New York Stock Exchange or debt rating agencies’ actions resulting therefrom;
- the possibility of adverse consequences of the pending securities litigation and on-going SEC investigations;
- we may be exposed to product liability and warranty claims if the use of our products results, or is alleged to result, in bodily injury and/or property damage or our products fail to perform as expected;
- the possibility of adverse consequences of governmental tax audits of our tax returns, including the IRS audit of our U.S. tax returns for the years 2002 through 2004;
- there are a substantial amount of outstanding stock options granted in past years to employees under the Company’s stock option plans which have been unexercisable for an extended period due to our non-current filing status of all our SEC financial reports. These include 809,667 options held by our former Chairman, President and Chief Executive Officer, C. Scott Greer. Given the significant increase in the Company’s share price during this exercise unavailability period, it is possible that many holders may want to exercise promptly when first able to do so. Once we regain both a current SEC financial report filing status and the ability to once again register our stock option shares with the SEC, we will reopen the stock option exercise program. We currently expect this reopening to occur in 2006. If the holders of a large number of these shares do then promptly exercise at this reopening, there would be some dilutive impact on the outstanding shares. We are still evaluating the impact of the reopening the stock option exercise program on our cash flows;
- the costs of energy, metal alloys, nickel and other raw materials have increased and our operating margins and results of operations could be adversely affected if we are unable to pass such increases on to our customers;
- our ability to convert bookings, which are not subject to nor computed in accordance with generally accepted accounting principles, into revenues at acceptable, if any, profit margins, since such profit margins cannot be assured nor be necessarily assumed to follow historical trends;
- our business depends on the levels of capital investment and maintenance expenditures by our customers, which in turn are affected by the cyclical nature of their markets and liquidity;
- work stoppages and other labor matters could adversely impact our business;
- changes in the financial markets and the availability of capital;
- we sell our products in highly competitive markets, which puts pressure on our profit margins and limits our ability to maintain or increase the market share of our products;
- we may not be able to continue to expand our market presence through acquisitions, and any future acquisitions may present unforeseen integration difficulties or costs;
- a substantial portion of our operations is conducted and located outside of the U.S. and economic, political and other risks associated with international operations could adversely affect our business in the U.S. and other countries and regions;
- our ability to comply with the laws and regulations affecting our international operations, including the U.S. export laws, and the effect of any noncompliance;

- political risks, military actions or trade embargoes affecting customer markets, including the continuing conflict in Iraq and its potential impact on Middle Eastern markets and global petroleum producers;
- the health of the petroleum, chemical, power and water industries;
- adverse movement in currency exchange rates;
- unanticipated difficulties or costs associated with the implementation of systems, including software;
- our relative geographical profitability and its impact on our ability to utilize foreign tax credits;
- the recognition of significant expenses associated with realigning operations of acquired companies with those of our company;
- our ability to meet the financial covenants and other restrictive covenants in our debt agreements may limit our operating and financial flexibility;
- the loss of services of any of our newly appointed and existing senior management or other key personnel could adversely affect our ability to implement our business strategy;
- any terrorist attacks and the response of the U.S. to such attacks or to the threat of such attacks;
- our ability to protect our intellectual property affects our competitive position;
- changes in prevailing interest rates and our effective interest costs; and
- adverse changes in the regulatory climate and other legal obligations imposed on our operations.

It is not possible to foresee or identify all the factors that may affect our future performance or any forward-looking information, and new risk factors can emerge from time to time. Given these risks and uncertainties, you should not place undue reliance on forward-looking statements as a prediction of actual results.

All forward-looking statement included in this Quarterly Report are based on information available to us on the date of this Quarterly Report. We undertake no obligation to revise our update any forward-looking statement or disclose any facts, events or circumstances that occur after the date hereof that may affect the accuracy of any forward-looking statement.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We have market risk exposure arising from changes in interest rates and foreign currency exchange rate movements.

Our earnings are impacted by changes in short-term interest rates as a result of borrowings under our 2000 Credit Facilities, which bear interest based on floating rates. At September 30, 2004, after the effect of interest rate swaps, we have approximately $400.1 million of variable rate debt obligations outstanding with a weighted average interest rate of 4.62%. A hypothetical change of 100-basis points in the interest rate for these borrowings, assuming constant variable rate debt levels, would have changed interest expense by approximately $3.0 million for the nine months ended September 30, 2004.

We are exposed to credit-related losses in the event of non-performance by counterparties to financial instruments including interest rate swaps, but we expect all counterparties to meet their obligations given their creditworthiness. As of September 30, 2004, we have $210 million of notional amount in outstanding interest rate swaps with third parties with maturities through June 2011 compared to $215 million as of the same period in 2003.

We employ a foreign currency hedging strategy to minimize potential losses in earnings or cash flows from unfavorable foreign currency exchange rate movements. These strategies also minimize potential gains from favorable exchange rate movements. Foreign currency exposures arise from transactions, including firm commitments and anticipated transactions, denominated in a currency other than an entity's functional currency and from foreign-denominated revenues and profits translated back into U.S. dollars. Based on a sensitivity analysis at September 30, 2004, a 10% adverse change in the foreign currency exchange rates could impact our results of operations for the nine months ended September 30, 2004 by $5.1 million as shown below:

(Amounts in millions)	
Euro	$ 2.2
Singapore dollar	0.7
Indian rupee	0.5
Venezuelan bolivar	0.3
Australian dollar	0.2
British pound	0.2
Mexican peso	0.2
Argentina peso	0.1
Swedish krona	0.1
All other	0.6
Total	$ 5.1

Exposures are hedged primarily with foreign currency forward contracts that generally have maturity dates less than one year. Company policy allows foreign currency coverage only for identifiable foreign currency exposures and, therefore, we do not enter into foreign currency contracts for trading purposes where the objective would be to generate profits. As of September 30, 2004, we have a U.S. dollar equivalent of $83.4 million in outstanding forward contracts with third parties compared with $73.0 million at September 30, 2003.

Generally, we view our investments in foreign subsidiaries from a long-term perspective, and therefore, do not hedge these investments. We use capital structuring techniques to manage our investment in foreign subsidiaries as deemed necessary.

We realized gains (losses) associated with foreign currency translation of $3.4 million and $(5.2) million for the three months ended September 30, 2004 and 2003, respectively, and $(11.0) million and $32.7 million for the nine months ended September 30, 2004 and 2003, respectively, which are included in other comprehensive income (loss). Transactional currency gains and losses arising from transactions outside of our sites' functional currencies and changes in fair value of forward contracts that do not qualify for hedge accounting are included in our consolidated results of operations. We realized foreign currency losses of $4.6 million and $1.0 million for the three months ended September 30, 2004 and 2003, respectively, and $10.5 million and $4.7 million for the nine months ended September 30, 2004 and 2003, respectively, which is included in other expense, net in the accompanying consolidated statements of operations. The currency losses in 2004 compared with 2003 reflect strengthening of the Euro and the Singapore dollar versus the U.S. dollar.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

Disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) are controls and other procedures that are designed to provide reasonable assurance that the information that we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

In connection with the preparation of this Quarterly Report, our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2004. In making this evaluation, our management considered the matters relating to our recently completed restatement of our financial statements and the material weaknesses described in our 2004 Annual Report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective at the reasonable assurance level as of September 30, 2004.

A material weakness is a control deficiency, or combination of control deficiencies, that result in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. As more fully described in “Management’s Report on Internal Control over Financial Reporting” in Item 9A of our 2004 Annual Report, management identified the following material weaknesses in our internal control over financial reporting as of December 31, 2004, which also existed as of September 30, 2004:

We did not maintain (1) an effective control environment, (2) effective monitoring controls to determine the adequacy of its internal control over financial reporting and related policies and procedures, (3) effective controls over certain of our period-end financial close and reporting processes, (4) effective segregation of duties over automated and manual transaction processes, (5) effective controls over the preparation, review and approval of account reconciliations, (6) effective controls over the complete and accurate recording and monitoring of intercompany accounts, (7) effective controls over the recording of journal entries, both recurring and non-recurring, (8) effective controls over the existence, completeness and accuracy of fixed assets and related depreciation and amortization expense, (9) effective controls over the completeness and accuracy of revenue, deferred revenue, accounts receivable and accrued liabilities, (10) effective controls over the completeness, accuracy, valuation and existence of our inventory and related cost of sales accounts, (11) effective controls over the completeness and accuracy of our reporting of certain non-U.S. pension plans, (12) effective controls over the complete and accurate recording of rights and obligations associated with our accounts receivable factoring and securitization transactions, (13) effective controls over our accounting for certain derivative transactions, (14) effective controls over our accounting for equity investments, (15) effective controls over our accounting for income taxes, including income taxes payable, deferred income tax assets and liabilities and the related income tax provision, (16) effective controls over our accounting for mergers and acquisitions, (17) effective controls over the completeness and accuracy of certain accrued liabilities and the related operating expense accounts, (18) effective controls over the completeness, accuracy and validity of payroll and accounts payable disbursements to ensure that they were adequately reviewed and approved prior to being recorded and reported, (19) effective controls over the completeness, accuracy and validity of spreadsheets used in our financial reporting process to ensure that access was restricted to appropriate personnel, and that unauthorized modification of the data or formulas within spreadsheets was prevented, and (20) effective controls over the accuracy, valuation and disclosure of our goodwill and intangible asset accounts and the related amortization and impairment expense accounts, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

In light of the material weaknesses in our 2004 Annual Report, we performed additional analyses and other procedures to ensure that our unaudited condensed consolidated financial statements included in this Quarterly Report were prepared in accordance with GAAP. As a result of these procedures, we believe that the unaudited condensed consolidated financial statements included in this Quarterly Report present fairly, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with GAAP.

Plan for Remediation of Material Weaknesses

In response to the identified material weaknesses, our management, with oversight from our audit committee, has dedicated significant resources, including the engagement of external consultants, to support management in its efforts to improve our control environment and to remedy the identified material weaknesses. As more fully described in our 2004 Annual Report, the ongoing remediation efforts subsequent to December 31, 2004 are focused on (i) expanding our organizational capabilities to improve our control environment; (ii) implementing process changes to strengthen our internal control and monitoring activities; and (iii) implementing adequate information technology general controls.

We believe that these remediation efforts have improved and will continue to improve our internal control over financial reporting, as well as our disclosure controls and procedures. However, not all of the material weaknesses described above and in our 2004 Annual Report will be remediated by December 31, 2005, our next reporting "as of" date under Sarbanes-Oxley Section 404. Accordingly, we expect to report that our internal control over financial reporting and our disclosure controls and procedures remain ineffective as of December 31, 2005.

Changes in Internal Control over Financial Reporting

There have been no material changes in our internal control over financial reporting during the three months ended September 30, 2004 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings.

We are a defendant in a large number of pending lawsuits (which include, in many cases, multiple claimants) that seek to recover damages for personal injury allegedly caused by exposure to asbestos containing products manufactured and/or distributed by us in the past. Any such products were encapsulated and used only as components of process equipment, and we do not believe that any emission of respirable asbestos fibers occurred during the use of this equipment. We believe that a high percentage of the applicable claims are covered by applicable insurance or indemnities from other companies.

On February 4, 2004, we received an informal inquiry from the SEC requesting the voluntary production of documents and information related to our February 3, 2004 announcement that we would restate our financial results for the nine months ended September 30, 2003 and the full years 2002, 2001 and 2000. On June 2, 2004, we were advised that the SEC had issued a formal order of private investigation into issues regarding this restatement and any other issues that arise from the investigation. We continue to cooperate with the SEC in this matter.

During the quarter ended September 30, 2003, related lawsuits were filed in federal court in the Northern District of Texas (the "Court''), alleging that we violated federal securities laws. Since the filing of these cases, which have been consolidated, the lead plaintiff has amended its complaint several times. The lead plaintiff's current pleading is the fifth consolidated amended complaint ("Complaint''). The Complaint alleges that federal securities violations occurred between February 6, 2001 and September 27, 2002 and names as defendants Mr. C. Scott Greer, our former Chairman, President and Chief Executive Officer, Ms. Renee J. Hornbaker, our former Vice President and Chief Financial Officer, PricewaterhouseCoopers LLP, our independent registered public accounting firm, and Banc of America Securities LLC and Credit Suisse First Boston LLC, which served as underwriters for two of our public stock offerings during the relevant period. The Complaint asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, and Sections 11 and 15 of the Securities Act of 1933. The lead plaintiff seeks unspecified compensatory damages, forfeiture by Mr. Greer and Ms. Hornbaker of unspecified incentive-based or equity-based compensation and profits from any stock sales, and recovery of costs. On November 22, 2005, the Court entered an order denying the defendants' motions to dismiss the Complaint on the pleadings in their entirety. The case is currently set for trial on March 27, 2007. We continue to believe that the lawsuit is without merit and are vigorously defending the case.

On October 6, 2005, a shareholder derivative lawsuit was filed purportedly on our behalf in the 193rd Judicial District of Dallas County, Texas. The lawsuit names as defendants Mr. Greer, Ms. Hornbaker, and current board members Hugh K. Coble, George T. Haymaker, Jr., William C. Rusnack, Michael F. Johnston, Charles M. Rampacek, Kevin E. Sheehan, Diane C. Harris, James O. Rollans and Christopher A. Bartlett. We are named as a nominal defendant. Based primarily on the purported misstatements alleged in the above-described federal securities case, the plaintiff asserts claims against the defendants for breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets and unjust enrichment. The plaintiff alleges that these purported violations of state law occurred between April 2000 and the date of suit. The plaintiff seeks on our behalf an unspecified amount of damages, injunctive relief and/or the imposition of a constructive trust on defendants' assets, disgorgement of compensation, profits or other benefits received by the defendants from us, and recovery of attorneys' fees and costs. We strongly believe that the suit was improperly filed and have filed a motion seeking dismissal of the case.

On February 7, 2006, we received a subpoena from the SEC regarding goods and services that we delivered to Iraq from 1996 through 2003 during the United Nations Oil-for-Food Program. We are in the process of reviewing and responding to the subpoena and intend to cooperate with the SEC. We believe that other companies in our industry (as well as in other industries) have received similar subpoenas and requests for information.

On March 14, 2006, a shareholder derivative lawsuit was filed purportedly on our behalf in federal court in the Northern District of Texas. The lawsuit names as defendants Mr. Greer, Ms. Hornbaker, and current board members Hugh K. Coble, George T. Haymaker, Jr., Lewis M. Kling, William C. Rusnack, Michael F. Johnston, Charles M. Rampacek, Kevin E. Sheehan, Diane C. Harris, James O. Rollans and Christopher A. Bartlett. We named as a nominal defendant. Based primarily on certain of the purported misstatements alleged in the above-described federal securities case, the plaintiff asserts claims against the defendants for breaches of fiduciary duty. The plaintiff alleges that the purported breaches of fiduciary duty occurred between 2000 and 2004. The plaintiff seeks on our behalf an unspecified amount of damages, disgorgement by Mr.

Greer and Ms. Hornbaker of salaries, bonuses, restricted stock and stock options, and recovery of attorneys' fees and costs. We strongly believe that the suit was improperly filed and intend to file a motion seeking dismissal of the case.

Since we manufacture and sell our products globally, we are subject to risks associated with doing business internationally. In March 2006, we initiated a process to determine our compliance posture with respect to U.S. export control laws and regulations. Upon initial investigation, it appears that some product transactions and technology transfers require further research to determine compliance with U.S. export control laws and regulations. With assistance from outside counsel, we are currently involved in a systematic process to conduct further research. Any potential violations of U.S. export control laws and regulations that are identified may result in civil or criminal penalties, including fines and/or suspension of the privilege to engage in export transactions or to have our foreign affiliates receive U.S.-origin goods, software or technology. Because our research into this issue is ongoing, we are unable to determine the extent of any violations or the nature or amount of any potential penalties to which we might be subject to in the future. As a result, we cannot currently predict whether the resolution of this matter will materially adversely affect our financial position or results of operations. At this time, we have not made any provision in our consolidated financial statements for any fines or penalties that might be incurred relating to this matter.

We have been involved as a potentially responsible party ("PRP'') at former public waste disposal sites that may be subject to remediation under pending government procedures. The sites are in various stages of evaluation by federal and state environmental authorities. The projected cost of remediation at these sites, as well as our alleged "fair share'' allocation, is uncertain and speculative until all studies have been completed and the parties have either negotiated an amicable resolution or the matter has been judicially resolved. At each site, there are many other parties who have similarly been identified, and the identification and location of additional parties is continuing under applicable federal or state law. Many of the other parties identified are financially strong and solvent companies that appear able to pay their share of the remediation costs. Based on our information about the waste disposal practices at these sites and the environmental regulatory process in general, we believe that it is likely that ultimate remediation liability costs for each site will be apportioned among all liable parties, including site owners and waste transporters, according to the volumes and/or toxicity of the wastes shown to have been disposed of at the sites. We believe that our exposure for existing disposal sites will be less than $100,000.

We are also a defendant in several other lawsuits, including product liability claims, that are insured, subject to the applicable deductibles, arising in the ordinary course of business. Based on currently available information, we believe that we have adequately accrued estimated probable losses for such lawsuits. We are also involved in a substantial number of labor claims, including one case where we had a confidential settlement reflected in our 2004 results.

Although none of the aforementioned potential liabilities can be quantified with absolute certainty, we have established reserves covering these exposures, which we believe to be reasonable based on past experience and available facts. While additional exposures beyond these reserves could exist, they currently cannot be estimated. We will continue to evaluate these potential contingent loss exposures and, if they develop, recognize expense as soon as such losses become probable and can be reasonably estimated.

We are also involved in ordinary routine litigation incidental to our business, none of which we believe to be material to our business, operations or overall financial condition. However, resolutions or dispositions of claims or lawsuits by settlement or otherwise could have a significant impact on our operating results for the reporting period in which any such resolution or disposition occurs.

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Item 6. Exhibits.

Set forth below is a list of exhibits included as part of this Quarterly Report:

Exhibit No.	Description
3.1	1988 Restated Certificate of Incorporation of The Duriron Company, Inc., filed as Exhibit 3.1 to Flowserve Corporation's (f/k/a The Duriron Company) Annual Report on Form 10-K for the year ended December 31, 1988.
3.2	1989 Amendment to Certificate of Incorporation, filed as Exhibit 3.2 to Flowserve Corporation's Annual Report on Form 10-K for the year ended December 31, 1989.
3.3	1996 Certificate of Amendment of Certificate of Incorporation, filed as Exhibit 3.4 to Flowserve Corporation's Annual Report on Form 10-K for the year ended December 31, 1995.
3.4	April 1997 Certificate of Amendment of Certificate of Incorporation, filed as part of Annex VI to the Joint Proxy Statement/ Prospectus, which is part of Flowserve Corporation's Registration Statement on Form S-4, dated June 19, 1997.
3.5	July 1997 Certificate of Amendment of Certificate of Incorporation, filed as Exhibit 3.6 to Flowserve Corporation's Quarterly Report on Form 10-Q, for the quarter ended June 30, 1997.
3.6	Amended and Restated By-Laws of Flowserve Corporation, as amended, filed as Exhibit 3.9 to Flowserve Corporation's Annual Report on Form 10-K for the year ended December 31, 2003.
10.1	Letter Amendment to Finance Contract, dated July 2, 2004, among Flowserve Corporation, Flowserve B.V. and European Investment Bank, filed as Exhibit 10.6 to Flowserve Corporation's Current Report on Form 8-K, dated March 18, 2005.
10.2	Letter of Credit and Reimbursement Agreement, dated July 28, 2004, among Flowserve B.V., Calyon New York Branch, as administrative agent and issuing lender, and the other lenders named therein, as amended March 15, 2005, filed as Exhibit 10.7 to Flowserve Corporation's Current Report on Form 8-K, dated March 18, 2005. [1]
31.1	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

[1] The Letter of Credit and Reimbursement Agreement was subsequently amended by that certain First Amendment and Limited Waiver to Letter of Credit and Reimbursement Agreement, dated March 15, 2005, filed as Exhibit 10.8 to Flowserve Corporation's Current Report on Form 8-K, dated March 18, 2005. The Letter of Credit and Reimbursement Agreement, as amended, was terminated on August 12, 2005.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FLOWSERVE CORPORATION
(Registrant)

Date: April 26, 2006

/s/ Lewis M. Kling
Lewis M. Kling
President and Chief Executive Officer

Date: April 26, 2006

/s/ Mark A. Blinn
Mark A. Blinn
Vice President and Chief Financial Officer

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EXHIBIT 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

I, Lewis M. Kling, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Flowserve Corporation;

2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Quarterly Report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: April 26, 2006

/s/ Lewis M. Kling

Lewis M. Kling
President and
Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

I, Mark A. Blinn, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Flowserve Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Quarterly Report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Quarterly Report based on such evaluation; and

(d) Disclosed in this Quarterly Report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: April 26, 2006

/s/ Mark A. Blinn

Mark A. Blinn
Vice President and
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Flowserve Corporation (the “Company”) on Form 10-Q for the period ended September 30, 2004 (the “Quarterly Report”), I, Lewis M. Kling, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Lewis M. Kling

Lewis M. Kling
President and
Chief Executive Officer

Date: April 26, 2006

EXHIBIT 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Flowserve Corporation (the "Company") on Form 10-Q for the period ended September 30, 2004 (the "Quarterly Report"), I, Mark A. Blinn, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Mark A. Blinn

Mark A. Blinn
Vice President and
Chief Financial Officer

Date: April 26, 2006