

PENTAIR INC  
Form 10-Q  
October 21, 2008

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the Quarterly Period Ended September 27, 2008**

**OR**

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

**Commission file number 000-04689**

**Pentair, Inc.**

**(Exact name of Registrant as specified in its charter)**

**Minnesota**

**41-0907434**

**(State or other jurisdiction of incorporation or organization)**

**(I.R.S. Employer Identification number)**

**5500 Wayzata Blvd, Suite 800, Golden Valley,  
Minnesota**

**55416**

**(Address of principal executive offices)**

**(Zip code)**

**Registrant's telephone number, including area code: (763) 545-1730**

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, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

On September 27, 2008, 98,629,464 shares of Registrant's common stock were outstanding.

**Pentair, Inc. and Subsidiaries**

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**Table of Contents****PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****Pentair, Inc. and Subsidiaries  
Condensed Consolidated Statements of Income (Unaudited)**

|  | <b>Three months ended</b>        |                                  | <b>Nine months ended</b>     |                              |
|--|----------------------------------|----------------------------------|------------------------------|------------------------------|
|  | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> | <b>September 27<br/>2008</b> | <b>September 29<br/>2007</b> |
| <i>In thousands, except per-share data</i>                                     |                                  |                                  |                              |                              |
| Net sales  | \$864,167                        | \$821,215                        | \$2,614,328                  | \$2,513,359                  |
| Cost of goods sold   | 608,854                          | 576,519                          | 1,829,622                    | 1,753,183                    |
| Gross profit   | 255,313                          | 244,696                          | 784,706                      | 760,176                      |
| Selling, general and administrative  | 154,972                          | 137,100                          | 439,929                      | 428,463                      |
| Research and development   | 16,691                           | 14,446                           | 48,871                       | 44,204                       |
| Legal settlement   |                                  |                                  | 20,435                       |                              |
| Operating income   | 83,650                           | 93,150                           | 275,471                      | 287,509                      |
| Other (income) expense:  |                                  |                                  |                              |                              |
| Gain on sale of interest in subsidiaries                                       |                                  |                                  | (109,648)                    |                              |
| Equity losses of unconsolidated subsidiary                                     | 669                              | 845                              | 2,433                        | 1,838                        |
| Loss on early extinguishment of debt   | 4,611                            |                                  | 4,611                        |                              |
| Net interest expense   | 13,735                           | 18,157                           | 45,685                       | 51,351                       |
| Income from continuing operations before<br>income taxes and minority interest | 64,635                           | 74,148                           | 332,390                      | 234,320                      |
| Provision for income taxes   | 21,146                           | 14,869                           | 97,522                       | 71,419                       |
| Minority Interest  | 2,100                            |                                  | 2,100                        |                              |
| Income from continuing operations  | 41,389                           | 59,279                           | 232,768                      | 162,901                      |
| Loss from discontinued operations, net of tax                                  |                                  | (1,235)                          | (1,217)                      | (726)                        |
| Gain (loss) on disposal of discontinued<br>operations, net of tax              | (269)                            |                                  | (7,406)                      | 207                          |
| Net income   | \$ 41,120                        | \$ 58,044                        | \$ 224,145                   | \$ 162,382                   |
| <b>Earnings (loss) per common share</b>  |                                  |                                  |                              |                              |
| <b>Basic</b>   |                                  |                                  |                              |                              |
| Continuing operations  | \$ 0.42                          | \$ 0.60                          | \$ 2.37                      | \$ 1.65                      |
| Discontinued operations  |                                  | (0.01)                           | (0.08)                       | (0.01)                       |
| Basic earnings per common share  | \$ 0.42                          | \$ 0.59                          | \$ 2.29                      | \$ 1.64                      |
| <b>Diluted</b>   |                                  |                                  |                              |                              |
| Continuing operations  | \$ 0.42                          | \$ 0.59                          | \$ 2.34                      | \$ 1.63                      |
| Discontinued operations  |                                  | (0.01)                           | (0.08)                       | (0.01)                       |

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|   |         |         |         |         |
|---|---------|---------|---------|---------|
| Diluted earnings per common share                 | \$ 0.42 | \$ 0.58 | \$ 2.26 | \$ 1.62 |
| <b>Weighted average common shares outstanding</b> |         |         |         |         |
| Basic   | 97,827  | 98,747  | 98,049  | 98,859  |
| Diluted   | 99,319  | 100,365 | 99,372  | 100,339 |
| <b>Cash dividends declared per common share</b>   | \$ 0.17 | \$ 0.15 | \$ 0.51 | \$ 0.45 |

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**Pentair, Inc. and Subsidiaries**  
**Condensed Consolidated Balance Sheets (Unaudited)**

| <i>In thousands, except share and per-share data</i> | <b>September 27<br/>2008</b> | <b>December 31<br/>2007</b> | <b>September 29<br/>2007</b> |
|--|------------------------------|-----------------------------|------------------------------|
| <b>Assets</b>  |                              |                             |                              |
| <b>Current assets</b>                                |                              |                             |                              |
| Cash and cash equivalents                            | \$ 93,544                    | \$ 70,795                   | \$ 56,555                    |
| Accounts and notes receivable, net                   | 517,240                      | 466,675                     | 473,496                      |
| Inventories  | 430,386                      | 392,416                     | 395,638                      |
| Deferred tax assets                                  | 50,061                       | 50,511                      | 52,038                       |
| Prepaid expenses and other current assets            | 53,504                       | 35,908                      | 47,746                       |
| Current assets of discontinued operations            |                              | 21,716                      | 26,868                       |
| <b>Total current assets</b>                          | <b>1,144,735</b>             | <b>1,038,021</b>            | <b>1,052,341</b>             |
| <b>Property, plant and equipment, net</b>            | <b>363,352</b>               | <b>365,990</b>              | <b>356,594</b>               |
| <b>Other assets</b>                                  |                              |                             |                              |
| Goodwill   | 2,134,031                    | 2,004,720                   | 1,989,620                    |
| Intangibles, net                                     | 539,133                      | 491,263                     | 492,732                      |
| Other  | 69,874                       | 82,237                      | 77,084                       |
| Non-current assets of discontinued operations        |                              | 18,383                      | 18,500                       |
| <b>Total other assets</b>                            | <b>2,743,038</b>             | <b>2,596,603</b>            | <b>2,577,936</b>             |
| <b>Total assets</b>                                  | <b>\$4,251,125</b>           | <b>\$4,000,614</b>          | <b>\$3,986,871</b>           |
| <b>Liabilities and Shareholders Equity</b>           |                              |                             |                              |
| <b>Current liabilities</b>                           |                              |                             |                              |
| Short-term borrowings                                | \$                           | \$ 13,586                   | \$ 4,800                     |
| Current maturities of long-term debt                 | 3,913                        | 5,075                       | 4,992                        |
| Accounts payable                                     | 225,928                      | 229,937                     | 204,360                      |
| Employee compensation and benefits                   | 107,163                      | 111,475                     | 107,271                      |
| Current pension and post-retirement benefits         | 8,557                        | 8,557                       | 7,918                        |
| Accrued product claims and warranties                | 43,012                       | 49,382                      | 47,719                       |
| Income taxes   | 7,806                        | 12,919                      | 10,862                       |
| Accrued rebates and sales incentives                 | 35,907                       | 36,663                      | 36,910                       |
| Other current liabilities                            | 101,662                      | 90,377                      | 111,833                      |
| Current liabilities of discontinued operations       |                              | 2,935                       | 5,431                        |
| <b>Total current liabilities</b>                     | <b>533,948</b>               | <b>560,906</b>              | <b>542,096</b>               |
| <b>Other liabilities</b>                             |                              |                             |                              |
| Long-term debt                                       | 1,035,150                    | 1,041,925                   | 1,102,707                    |
| Pension and other retirement compensation            | 164,776                      | 161,042                     | 222,098                      |

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|  |                    |                    |                    |
|--|--------------------|--------------------|--------------------|
| Post-retirement medical and other benefits   | 34,218             | 37,147             | 46,499             |
| Long-term income taxes payable   | 25,356             | 21,306             | 18,214             |
| Deferred tax liabilities   | 184,514            | 167,633            | 134,683            |
| Other non-current liabilities  | 96,941             | 97,086             | 89,898             |
| Non-current liabilities of discontinued operations   |                    | 2,698              | 2,519              |
| <b>Total liabilities</b>   | <b>2,074,903</b>   | <b>2,089,743</b>   | <b>2,158,714</b>   |
| Commitments and contingencies  |                    |                    |                    |
| <b>Minority interest</b>   | <b>120,230</b>     |                    |                    |
| <b>Shareholders equity</b>   |                    |                    |                    |
| Common shares par value \$0.16 <sup>2/3</sup> ; 98,629,464, 99,221,831<br>and 99,468,474 shares issued and outstanding, respectively | 16,438             | 16,537             | 16,578             |
| Additional paid-in capital   | 456,144            | 476,242            | 478,396            |
| Retained earnings  | 1,469,830          | 1,296,226          | 1,262,604          |
| Accumulated other comprehensive income   | 113,580            | 121,866            | 70,579             |
| <b>Total shareholders equity</b>   | <b>2,055,992</b>   | <b>1,910,871</b>   | <b>1,828,157</b>   |
| <b>Total liabilities and shareholders equity</b>   | <b>\$4,251,125</b> | <b>\$4,000,614</b> | <b>\$3,986,871</b> |

*See accompanying notes to condensed consolidated financial statements.*

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**Pentair, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Cash Flows (Unaudited)**

|  | <b>Nine months ended</b> |                     |
|--|--------------------------|---------------------|
|  | <b>September 27</b>      | <b>September 29</b> |
| <i>In thousands</i>  | <b>2008</b>              | <b>2007</b>         |
| <b>Operating activities</b>  |                          |                     |
| Net income   | \$ 224,145               | \$ 162,382          |
| <b>Adjustments to reconcile net income to net cash provided by (used for) operating activities</b> |                          |                     |
| Loss from discontinued operations  | 1,217                    | 726                 |
| (Gain) loss on disposal of discontinued operations   | 7,406                    | (207)               |
| Equity losses of unconsolidated subsidiary   | 2,433                    | 1,838               |
| Minority interest  | 2,100                    |                     |
| Depreciation   | 45,759                   | 45,538              |
| Amortization   | 20,220                   | 18,635              |
| Deferred income taxes  | 25,927                   | (18,883)            |
| Stock compensation   | 15,948                   | 17,071              |
| Excess tax benefits from stock-based compensation  | (1,617)                  | (2,706)             |
| Gain on sale of assets   | 87                       | (2,195)             |
| Gain on sale of interest in subsidiaries   | (109,648)                |                     |
| <b>Changes in assets and liabilities, net of effects of business acquisitions and dispositions</b> |                          |                     |
| Accounts and notes receivable  | (55,727)                 | (27,927)            |
| Inventories  | (26,518)                 | 13,973              |
| Prepaid expenses and other current assets  | (15,798)                 | (8,681)             |
| Accounts payable   | 1,343                    | (1,088)             |
| Employee compensation and benefits   | (7,471)                  | 3,037               |
| Accrued product claims and warranties  | (6,483)                  | 3,199               |
| Income taxes   | (5,792)                  | (4,573)             |
| Other current liabilities  | 9,380                    | 15,955              |
| Pension and post-retirement benefits   | 592                      | 7,924               |
| Other assets and liabilities   | 13,146                   | 7,396               |
| Net cash provided by (used for) continuing operations  | 140,649                  | 231,414             |
| Net cash provided by ( used for) operating activities of discontinued operations                   | (3,432)                  | (2,081)             |
| Net cash provided by (used for) operating activities   | 137,217                  | 229,333             |
| <b>Investing activities</b>  |                          |                     |
| Capital expenditures   | (40,107)                 | (45,163)            |
| Proceeds from sale of property and equipment   | 4,304                    | 5,136               |
| Acquisitions, net of cash acquired   | (1,609)                  | (486,264)           |
| Divestitures   | 29,526                   |                     |
| Other  | (7)                      | (4,044)             |
| Net cash provided by (used for) investing activities   | (7,893)                  | (530,335)           |



|   |           |           |
|---|-----------|-----------|
| <b>Financing activities</b>   |           |           |
| Net short-term borrowings   | (14,180)  | (10,378)  |
| Proceeds from long-term debt  | 479,405   | 1,147,132 |
| Repayment of long-term debt   | (486,492) | (770,822) |
| Debt issuance costs   | (114)     | (1,876)   |
| Excess tax benefits from stock-based compensation                   | 1,617     | 2,706     |
| Proceeds from exercise of stock options                             | 5,140     | 5,512     |
| Repurchases of common stock   | (37,342)  | (27,119)  |
| Dividends paid  | (50,541)  | (44,986)  |
| Net cash provided by (used for) financing activities                | (102,507) | 300,169   |
| <b>Effect of exchange rate changes on cash and cash equivalents</b> | (4,068)   | 2,568     |
| <b>Change in cash and cash equivalents</b>                          | 22,749    | 1,735     |
| <b>Cash and cash equivalents, beginning of period</b>               | 70,795    | 54,820    |
| <b>Cash and cash equivalents, end of period</b>                     | \$ 93,544 | \$ 56,555 |

*See accompanying notes to condensed consolidated financial statements.*

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****1. Basis of Presentation and Responsibility for Interim Financial Statements**

We prepared the unaudited condensed consolidated financial statements following the requirements of the Securities and Exchange Commission ( SEC ) for interim reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by accounting principles generally accepted in the United States can be condensed or omitted.

We are responsible for the unaudited financial statements included in this document. The financial statements include all normal recurring adjustments that are considered necessary for the fair presentation of our financial position and operating results. As these are condensed financial statements, one should also read our consolidated financial statements and notes thereto, which are included in our 2007 Annual Report on Form 10-K for the year ended December 31, 2007.

Certain line items within the 2007 Condensed Consolidated Statements of Income and the Condensed Consolidated Statements of Cash Flows have been reclassified from the 2007 presentation to conform to the 2008 presentation. The reclassification reflects the presentation of *Equity losses of unconsolidated subsidiary* of \$0.8 million and \$1.8 million for the three and nine months ended September 29, 2007, respectively, as a separate line item below *Operating income* in the Condensed Consolidated Statements of Income rather than as a component of *Selling, general and administrative*, and as a separate line in the *Adjustments to reconcile net income to net cash provided by( used for) by operating activities* in the Condensed Consolidated Statements of Cash Flows, rather than as a component of *Other assets and liabilities*. This reclassification corrects the previous presentation and was not material to the financial statements. It did not affect *Net income* within the Condensed Consolidated Statements of Income or net cash provided by (used for) operating, investing or financing activities within the Condensed Consolidated Statements of Cash Flows.

Revenues, expenses, cash flows, assets and liabilities can and do vary during each quarter of the year. Therefore, the results and trends in these interim financial statements may not be indicative of those for a full year.

Our fiscal year ends on December 31. We report our interim quarterly periods on a 13-week basis ending on a Saturday.

**2. New Accounting Standards**

In March 2008, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 161, *Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB statement No. 133* ( SFAS 161 ). SFAS 161 expands the disclosure requirements in Statement 133 about an entity's derivative instruments and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We are currently evaluating the impact of adopting SFAS 161.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB 51* ( SFAS 160 ). SFAS 160 changes the accounting and reporting for minority interests. Minority interests will be recharacterized as noncontrolling interests and will be reported as a component of equity separate from the parent's equity, and purchases or sales of equity interests that do not result in a change in control will be accounted for as equity transactions. In addition, net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement and upon a loss of control, the interest sold, as well as any interest retained, will be recorded at fair value with any gain or loss recognized in earnings. SFAS 160 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years, except for the presentation and disclosure requirements, which will apply retrospectively. Upon adoption, we will classify minority interest as a component of equity for all periods presented.

In December 2007, the FASB issued SFAS No. 141 (Revised 2007), *Business Combinations* ( SFAS 141R ). SFAS 141R replaces SFAS No. 141. SFAS 141R retains the purchase method of accounting for acquisitions, but requires a number of changes, including changes in the way assets and liabilities are recognized in the purchase accounting. SFAS 141R also changes the recognition of assets acquired and liabilities assumed arising from contingencies, requires the capitalization of in-process research and development at fair value, and requires the expensing of acquisition-related costs as incurred. SFAS 141R is effective for business combinations for which the acquisition date

is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. We will apply SFAS 141R prospectively to business combinations completed on or after that date. We do not expect adoption to have a significant impact to our current consolidated results of operations and financial condition.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value ( the Fair Value Option ). SFAS 159 is effective for fiscal years beginning after November 15, 2007. We did not choose the Fair Value Option; therefore, the adoption of SFAS 159 did not have any impact on our consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007, with the exception of the application of the statement to the determination of fair value of nonfinancial assets and liabilities that are recognized or disclosed on a nonrecurring basis, which is effective for fiscal years beginning after November 15, 2008.

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

SFAS 157 establishes a valuation hierarchy for disclosure of the inputs to valuation used to measure fair value. This hierarchy prioritizes the inputs into three broad levels as follows. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. Level 3 inputs are unobservable inputs based upon our own assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level of input that is significant to the fair value measurement.

At September 27, 2008, our interest rate swaps (see note 12) are carried at fair value measured on a recurring basis. Fair values are determined through the use of models that consider various assumptions, including time value, yield curves, as well as other relevant economic measures, which are inputs that are classified as Level 2 in the valuation hierarchy.

**3. Stock-based Compensation**

Total stock-based compensation expense was \$4.1 million and \$4.4 million for the three months ended September 27, 2008 and September 29, 2007, respectively, and was \$16.0 million and \$17.0 million for the nine months ended September 27, 2008 and September 29, 2007, respectively.

Non-vested shares of our common stock were granted to eligible employees with a vesting period of two to five years after issuance. Non-vested share awards are valued at market value on the date of grant and are typically expensed over the vesting period. Total compensation expense for non-vested share awards was \$2.0 million for the three months ended September 27, 2008 and September 29, 2007, respectively, and was \$7.5 million and \$7.4 million for the nine months ended September 27, 2008 and September 29, 2007, respectively.

During the first nine months of 2008, option awards were granted under the Omnibus Stock Incentive Plan, the 2008 Omnibus Stock Incentive Plan, as amended, and the Outside Directors Nonqualified Stock Option Plan (together the Plans), each with an exercise price equal to the market price of our common stock on the date of grant. Total compensation expense for stock option awards was \$2.1 million and \$2.4 million for the three months ended September 27, 2008 and September 29, 2007, respectively, and was \$8.5 million and \$9.6 million for the nine months ended September 27, 2008 and September 29, 2007, respectively.

We estimated the fair value of each stock option award on the date of grant using a Black-Scholes option pricing model, modified for dividends and using the following assumptions:

|                                 | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> |
|---------------------------------|----------------------------------|----------------------------------|
| Expected stock price volatility | 27.0%                            | 28.5%                            |
| Expected life                   | 4.8 yrs                          | 4.8 yrs                          |
| Risk-free interest rate         | 3.11%                            | 4.46%                            |
| Dividend yield                  | 1.90%                            | 1.66%                            |

The weighted-average fair value of options granted during the third quarter of 2008 and 2007 was \$8.35 and \$8.38 per share, respectively.

These estimates require us to make assumptions based on historical results, observance of trends in our stock price, changes in option exercise behavior, future expectations and other relevant factors. If other assumptions had been used, stock-based compensation expense, as calculated and recorded under SFAS No. 123R (revised 2004), *Share Based Payment*, (SFAS 123R) could have been affected.

We based the expected life assumption on historical experience as well as the terms and vesting periods of the options granted. For purposes of determining expected volatility, we considered a rolling average of historical volatility measured over a period approximately equal to the expected option term. The risk-free rate for periods that coincide

with the expected life of the options is based on the U.S. Treasury Department yield curve in effect at the time of grant.

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****4. Earnings Per Common Share**

Basic and diluted earnings per share were calculated using the following:

|   | Three months ended      |                         | Nine months ended       |                         |
|---|-------------------------|-------------------------|-------------------------|-------------------------|
|   | September<br>27<br>2008 | September<br>29<br>2007 | September<br>27<br>2008 | September<br>29<br>2007 |
| <i>In thousands</i>   |                         |                         |                         |                         |
| <b>Weighted average common shares<br/>outstanding basic</b>   | 97,827                  | 98,747                  | 98,049                  | 98,859                  |
| Dilutive impact of stock options and restricted<br>stock      | 1,492                   | 1,618                   | 1,323                   | 1,480                   |
| <b>Weighted average common shares<br/>outstanding diluted</b> | 99,319                  | 100,365                 | 99,372                  | 100,339                 |

Stock options excluded from the calculation of diluted earnings per share because the exercise price was greater than the average market price of the common shares

|  |       |       |       |       |
|--|-------|-------|-------|-------|
|  | 3,503 | 2,099 | 4,594 | 2,769 |
|--|-------|-------|-------|-------|

In December 2007, the Board of Directors authorized the repurchase of shares of our common stock during 2008 up to a maximum dollar limit of \$50 million. As of September 27, 2008, we had purchased 1,094,059 shares for \$38.1 million pursuant to this authorization during 2008. This authorization expires on December 31, 2008.

**5. Restructuring**

During the second quarter of 2008, we announced and initiated certain business restructuring initiatives to further streamline our operations as a result of continuing deterioration in certain end markets. In relation to these initiatives, we recorded restructuring charges (reflected in *Selling, general and administrative* expense on the accompanying Condensed Consolidated Statements of Income) of \$2.7 million primarily for severance benefits paid or to be paid to terminated employees.

During the third quarter of 2008, we announced and initiated additional business restructuring initiatives aimed at reducing our fixed cost structure and rationalizing our manufacturing footprint. These initiatives included the announcement of the closure of certain manufacturing facilities as well as the reduction in hourly and salaried headcount of approximately 850 employees principally within the Water Group. These actions will generally be completed by the end of 2009. Restructuring related costs included in *Selling, general and administrative* expenses on the Condensed Consolidated Statements of Income include costs for severance and related benefits, asset impairment charges and other restructuring costs.

Restructuring costs are summarized as follows:

|                             | Three months ended      |                         | Nine months ended       |                         |
|-----------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|                             | September<br>27<br>2008 | September<br>29<br>2007 | September<br>27<br>2008 | September<br>29<br>2007 |
| <i>In thousands</i>         |                         |                         |                         |                         |
| Severance and related costs | \$10,899                | \$                      | \$13,583                | \$                      |
| Asset impairment            | 4,600                   |                         | 4,600                   |                         |

|                           |          |    |          |    |
|---------------------------|----------|----|----------|----|
| Total restructuring costs | \$15,499 | \$ | \$18,183 | \$ |
|---------------------------|----------|----|----------|----|

Restructuring accrual activity is summarized as follows:

*In thousands*

|                               |  |  |  |          |
|-------------------------------|--|--|--|----------|
| Balance at March 29, 2008     |  |  |  | \$       |
| Costs incurred                |  |  |  | 2,684    |
| Cash payments                 |  |  |  | (723)    |
| Balance at June 28, 2008      |  |  |  | \$ 1,961 |
| Costs incurred                |  |  |  | 10,899   |
| Cash Payments                 |  |  |  | (3,338)  |
| Balance at September 27, 2008 |  |  |  | \$ 9,522 |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****6. Acquisitions**

On June 28, 2008, we entered into a transaction with GE Water & Process Technologies (a unit of General Electric Company) ( GE ) that was accounted for as an acquisition of an 80.1 percent ownership interest in GE s global water softener and residential water filtration business in exchange for a 19.9 percent interest in our global water softener and residential water filtration business (the GE Transaction ). The acquisition was effected through the formation of two new entities, a U.S. entity and an international entity, into which we and GE contributed certain assets, properties, liabilities and operations representing our respective global water softener and residential water filtration businesses. We are an 80.1 percent owner of the new entities and GE is a 19.9 percent owner. The fair value of the acquisition was \$228.9 million, which includes approximately \$2.9 million of acquisition related costs. The acquisition and related sale of our 19.9 percent interest resulted in a gain of \$109.6 million (\$85.8 million after tax), representing the difference between the carrying amount and the fair value of the 19.9 percent interest sold.

With the formation of this business, we believe we will be better positioned to serve residential customers with industry-leading technical applications in the areas of water conditioning, whole house filtration, point of use water management and water sustainability and expect to accelerate revenue growth by selling GE s existing residential conditioning products through our sales channels.

The fair value of the business acquired was allocated to the assets acquired and liabilities assumed based on their estimated fair values. The excess of the fair value acquired over the identifiable assets acquired and liabilities assumed is reflected as goodwill. Goodwill recorded as part of the purchase price allocation was approximately \$137.5 million. We continue to evaluate the purchase price allocation, including tangible and intangible assets, which primarily consist of trademarks, proprietary technology and customer relationships, contingent liabilities and liabilities associated with exit or disposal activities, and expect to revise the purchase price allocation in future periods as these estimates are finalized. The following table represents the preliminary purchase price allocation:

| <i>In thousands</i>            | <b>September 27,<br/>2008</b> |
|--------------------------------|-------------------------------|
| Inventory                      | \$ 12,188                     |
| Property, plant & equipment    | 12,934                        |
| Goodwill                       | 137,542                       |
| Identifiable intangible assets | 66,483                        |
| Current liabilities            | (234)                         |
|                                | <b>\$ 228,913</b>             |

On May 7, 2007, we acquired as part of our Technical Products Group the assets of Calmark Corporation ( Calmark ). Calmark s results of operations have been included in our condensed consolidated financial statements since the date of acquisition.

On April 30, 2007, we acquired as part of our Water Group all of the capital interests in Porous Media Corporation and Porous Media, Ltd. (together, Porous Media ). Porous Media s results of operations have been included in our condensed consolidated financial statements since the date of acquisition.

On February 2, 2007, we acquired as part of our Water Group all of the outstanding shares of capital stock of Jung Pumpen GmbH ( Jung Pump ). Jung Pump s results of operations have been included in our condensed consolidated financial statements since the date of acquisition.

The following pro forma condensed financial results of operations are presented as if the acquisitions described above had been completed at the beginning of the period.



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|  | <b>Three months ended</b>        |                                  | <b>Nine months ended</b>         |                                  |
|--|----------------------------------|----------------------------------|----------------------------------|----------------------------------|
|  | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> |
| <i>In thousands, except share and per-share data</i>             |                                  |                                  |                                  |                                  |
| Pro forma net sales from continuing operations                   | \$ 864,167                       | \$ 842,740                       | \$ 2,668,801                     | \$ 2,601,906                     |
| Pro forma net income from continuing operations                  | 41,389                           | 59,279                           | 232,768                          | 162,714                          |
| Income (loss) from discontinued operations, net of tax           | (269)                            | (1,235)                          | (8,623)                          | (519)                            |
| Pro forma net income   | 41,120                           | 58,044                           | 224,145                          | 162,195                          |
| <b>Pro forma earnings per common share continuing operations</b> |                                  |                                  |                                  |                                  |
| Basic  | \$ 0.42                          | \$ 0.60                          | \$ 2.37                          | \$ 1.65                          |
| Diluted  | \$ 0.42                          | \$ 0.59                          | \$ 2.34                          | \$ 1.63                          |

**Weighted average common shares outstanding**

|         |        |         |        |         |
|---------|--------|---------|--------|---------|
| Basic   | 97,827 | 98,747  | 98,049 | 98,859  |
| Diluted | 99,319 | 100,365 | 99,372 | 100,339 |

These pro forma condensed consolidated financial results have been prepared for comparative purposes only and include certain adjustments, such as increased interest expense on acquisition debt. They do not reflect the effect of costs or synergies that would have been expected to result from the integration of these acquisitions. The pro forma information does not purport to be indicative of the results of operations that actually would have resulted had the combination occurred at the beginning of each period presented, or of future results of the consolidated entities.

**7. Discontinued Operations**

In February 2008, consistent with our strategy to refine our portfolio and more fully focus on our core pool equipment business globally within our Water Group, we sold our National Pool Tile ( NPT ) business to Pool Corporation in a cash transaction for approximately \$30.0 million subject to certain price adjustments. NPT is a wholesale distributor of pool tile and composite pool finishes serving professional contractors in the swimming pool refurbish and construction markets. The results of NPT have been reported as discontinued operations for all periods presented. The assets and liabilities of NPT have been reclassified as discontinued operations for all periods presented.

Operating results of the discontinued operations for the third quarter of 2008 and 2007 are summarized below:

|  | <b>Three months ended</b>        |                                  | <b>Nine months ended</b>         |                                  |
|--|----------------------------------|----------------------------------|----------------------------------|----------------------------------|
|  | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> |
| <i>In thousands</i>  |                                  |                                  |                                  |                                  |
| Net sales  | \$                               | \$ 16,619                        | \$ 7,085                         | \$ 55,115                        |
| Income (loss) from discontinued operations before income taxes   |                                  | (2,008)                          | (1,965)                          | (1,187)                          |
| Income tax (expense) benefit                                     |                                  | 773                              | 748                              | 461                              |
| Income (loss) from discontinued operations, net of income taxes  |                                  | (1,235)                          | (1,217)                          | (726)                            |
| Gain (loss) on disposal of discontinued operations, before taxes | (433)                            |                                  | (7,021)                          | 325                              |

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|  |         |    |           |        |
|--|---------|----|-----------|--------|
| Income tax (expense) benefit                                   | 164     |    | (385)     | (118)  |
| Gain (loss) on disposal of discontinued operations, net of tax | \$(269) | \$ | \$(7,406) | \$ 207 |
|  | 10      |    |           |        |

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Net assets (liabilities) of discontinued operations consist of the following:

| <i>In thousands</i>                                | <b>December<br/>31<br/>2007</b> | <b>September<br/>29<br/>2007</b> |
|--|---------------------------------|----------------------------------|
| Accounts and notes receivable, net                 | \$ 5,547                        | \$ 6,419                         |
| Inventories  | 14,710                          | 18,664                           |
| Other current assets                               | 1,459                           | 1,785                            |
| Current assets of discontinued operations          | 21,716                          | 26,868                           |
| Property, plant and equipment, net                 | 1,436                           | 1,544                            |
| Goodwill   | 16,806                          | 16,806                           |
| Other non-current assets                           | 141                             | 150                              |
| Non-current assets of discontinued operations      | 18,383                          | 18,500                           |
| Total assets                                       | \$40,099                        | \$ 45,368                        |
| Accounts payable                                   | \$ 1,712                        | \$ 4,145                         |
| Other current liabilities                          | 1,223                           | 1,286                            |
| Current liabilities of discontinued operations     | 2,935                           | 5,431                            |
| Deferred income tax                                | 2,400                           | 2,203                            |
| Other non-current liabilities                      | 298                             | 316                              |
| Non-current liabilities of discontinued operations | 2,698                           | 2,519                            |
| Total liabilities                                  | 5,633                           | 7,950                            |
| Net assets of discontinued operations              | \$34,466                        | \$ 37,418                        |

**8. Inventories**

Inventories were comprised of:

| <i>In thousands</i>        | <b>September<br/>27<br/>2008</b> | <b>December 31<br/>2007</b> | <b>September<br/>29<br/>2007</b> |
|----------------------------|----------------------------------|-----------------------------|----------------------------------|
| Raw materials and supplies | \$216,185                        | \$ 199,330                  | \$ 199,876                       |
| Work-in-process            | 50,864                           | 51,807                      | 53,196                           |
| Finished goods             | 163,337                          | 141,279                     | 142,566                          |

|                   |           |           |           |
|-------------------|-----------|-----------|-----------|
| Total inventories | \$430,386 | \$392,416 | \$395,638 |
|-------------------|-----------|-----------|-----------|

### 9. Comprehensive Income

Comprehensive income and its components, net of tax, were as follows:

| <i>In thousands</i>  | <b>Three months ended</b>        |                                  | <b>Nine months ended</b>         |                                  |
|--|----------------------------------|----------------------------------|----------------------------------|----------------------------------|
|  | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> |
| Net income   | \$ 41,120                        | \$ 58,044                        | \$ 224,145                       | \$ 162,382                       |
| Changes in cumulative foreign currency translation adjustment                              | (55,594)                         | 27,952                           | (8,709)                          | 54,899                           |
| Changes in market value of derivative financial instruments classified as cash flow hedges | (931)                            | (2,336)                          | 423                              | (1,024)                          |
| Comprehensive income (loss)  | \$(15,405)                       | \$ 83,660                        | \$ 215,859                       | \$ 216,257                       |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****10. Goodwill and Other Intangible Assets**

Changes in the carrying amount of goodwill for the nine months ended September 27, 2008 and September 29, 2007 by segment were as follows:

| <i>In thousands</i>      | <b>December 31,<br/>2007</b> | <b>Acquisitions/Other</b> | <b>Foreign<br/>Currency<br/>Translation</b> | <b>September 27,<br/>2008</b> |
|--------------------------|------------------------------|---------------------------|---|-------------------------------|
| Water Group              | \$ 1,712,227                 | \$ 132,485                | \$ 1,270                                    | \$ 1,845,982                  |
| Technical Products Group | 292,493                      | (46)                      | (4,398)                                     | 288,049                       |
| Consolidated Total       | \$ 2,004,720                 | \$ 132,439                | \$ (3,128)                                  | \$ 2,134,031                  |

| <i>In thousands</i>      | <b>December 31,<br/>2006</b> | <b>Acquisitions/Other</b> | <b>Foreign<br/>Currency<br/>Translation</b> | <b>September 29,<br/>2007</b> |
|--------------------------|------------------------------|---------------------------|---|-------------------------------|
| Water Group              | \$ 1,432,653                 | \$ 248,531                | \$ 17,425                                   | \$ 1,698,609                  |
| Technical Products Group | 269,311                      | 11,543                    | 10,157                                      | 291,011                       |
| Consolidated Total       | \$ 1,701,964                 | \$ 260,074                | \$ 27,582                                   | \$ 1,989,620                  |

The increase in goodwill in the Water Group is related primarily to the GE Transaction in 2008 and our acquisitions of Jung Pump and Porous Media during 2007.

Intangible assets, other than goodwill, were comprised of:

| <i>In thousands</i>                | <b>September 27, 2008</b>            |                                     |            | <b>December 31, 2007</b>             |                                     |            | <b>September 29, 2007</b>            |                                     |            |
|------------------------------------|--------------------------------------|-------------------------------------|------------|--------------------------------------|-------------------------------------|------------|--------------------------------------|-------------------------------------|------------|
|                                    | <b>Gross<br/>carrying<br/>amount</b> | <b>Accumulated<br/>amortization</b> | <b>Net</b> | <b>Gross<br/>carrying<br/>amount</b> | <b>Accumulated<br/>amortization</b> | <b>Net</b> | <b>Gross<br/>carrying<br/>amount</b> | <b>Accumulated<br/>amortization</b> | <b>Net</b> |
| <b>Finite-life<br/>intangibles</b> |                                      |                                     |            |                                      |                                     |            |                                      |                                     |            |
| Patents                            | \$ 15,451                            | \$ (9,319)                          | \$ 6,132   | \$ 15,457                            | \$ (7,904)                          | \$ 7,553   | \$ 15,453                            | \$ (7,427)                          | \$ 8,026   |
| Non-compete<br>agreements          | 4,722                                | (4,454)                             | 268        | 4,722                                | (4,050)                             | 672        | 4,722                                | (3,686)                             | 1,036      |
| Brand names                        | 1,602                                | (40)                                | 1,562      |                                      |                                     |            |                                      |                                     |            |
| Proprietary<br>technology          | 73,462                               | (16,371)                            | 57,091     | 59,944                               | (12,564)                            | 47,380     | 59,863                               | (11,361)                            | 48,502     |
| Customer<br>relationships          | 289,872                              | (42,973)                            | 246,899    | 238,712                              | (30,378)                            | 208,334    | 236,340                              | (26,264)                            | 210,076    |
| Total<br>finite-life               | \$385,109                            | \$(73,157)                          | \$311,952  | \$318,835                            | \$(54,896)                          | \$263,939  | \$316,378                            | \$(48,738)                          | \$267,640  |

intangibles

**Indefinite-life  
intangibles**

|             |         |  |         |         |  |         |         |  |         |
|-------------|---------|--|---------|---------|--|---------|---------|--|---------|
| Brand names | 227,181 |  | 227,181 | 227,324 |  | 227,324 | 225,092 |  | 225,092 |
|-------------|---------|--|---------|---------|--|---------|---------|--|---------|

|                              |           |            |           |           |            |           |           |            |           |
|------------------------------|-----------|------------|-----------|-----------|------------|-----------|-----------|------------|-----------|
| Total<br>intangibles,<br>net | \$612,290 | \$(73,157) | \$539,133 | \$546,159 | \$(54,896) | \$491,263 | \$541,470 | \$(48,738) | \$492,732 |
|------------------------------|-----------|------------|-----------|-----------|------------|-----------|-----------|------------|-----------|

Intangible asset amortization expense was approximately \$5.9 million and \$4.7 million for the three months ended September 27, 2008 and September 29, 2007, respectively, and was approximately \$18.3 million and \$15.5 million for the nine months ended September 27, 2008 and September 29, 2007, respectively. The estimated future amortization expense for identifiable intangible assets during the remainder of 2008 and the next five years is as follows:

| <i>In thousands</i>               | <b>2008 Q4</b> | <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012</b> | <b>2013</b> |
|-----------------------------------|----------------|-------------|-------------|-------------|-------------|-------------|
| Estimated amortization<br>expense | \$6,735        | \$26,161    | \$25,488    | \$25,381    | \$24,374    | \$24,210    |

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**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****11. Debt**

Debt and the average interest rate on debt outstanding are summarized as follows:

| <i>In thousands</i>                                     | <b>Average<br/>interest rate<br/>September<br/>27, 2008</b> | <b>Maturity<br/>(Year)</b> | <b>September 27<br/>2008</b> | <b>December 31<br/>2007</b> | <b>September 29<br/>2007</b> |
|---|---|----------------------------|------------------------------|-----------------------------|------------------------------|
| Commercial paper  | 2.93%   |                            | \$ 25,392                    | \$ 105,990                  | \$ 179,772                   |
| Revolving credit facilities                             | 3.26%   | 2012                       | 267,900                      | 76,722                      | 63,475                       |
| Private placement fixed rate                            | 5.65%   | 2013-2017                  | 400,000                      | 400,000                     | 400,000                      |
| Private placement floating rate                         | 3.35%   | 2012-2013                  | 205,000                      | 205,000                     | 205,000                      |
| Senior notes  | 7.85%   | 2009                       | 133,900                      | 250,000                     | 250,000                      |
| Other   | 2.94%   | 2008-2016                  | 6,246                        | 20,387                      | 11,462                       |
| Total contractual debt obligations                      |   |                            | 1,038,438                    | 1,058,099                   | 1,109,709                    |
| Deferred income related to swaps                        |   |                            | 625                          | 2,487                       | 2,790                        |
| Total debt, including current portion per balance sheet |   |                            | 1,039,063                    | 1,060,586                   | 1,112,499                    |
| Less: Current maturities                                |   |                            | (3,913)                      | (5,075)                     | (4,992)                      |
| Short-term borrowings                                   |   |                            |                              | (13,586)                    | (4,800)                      |
| Long-term debt  |   |                            | \$1,035,150                  | \$1,041,925                 | \$1,102,707                  |

We have a multi-currency revolving Credit Facility ( Credit Facility ). The Credit Facility creates an unsecured, committed revolving credit facility of up to \$800 million, with multi-currency sub facilities to support investments outside the U.S. The Credit Facility expires on June 4, 2012. Borrowings under the Credit Facility will bear interest at the rate of LIBOR plus 0.50%. Interest rates and fees on the Credit Facility vary based on our credit ratings.

We are authorized to sell short-term commercial paper notes to the extent availability exists under the Credit Facility. We use the Credit Facility as back-up liquidity to support 100% of commercial paper outstanding. As of September 27, 2008, we had \$25.4 million of commercial paper outstanding that matures within 34 days. All of the commercial paper was classified as long-term as we have the intent and the ability to refinance such obligations on a long-term basis under the Credit Facility.

Total availability under our existing Credit Facility was \$506.7 million at September 27, 2008.

In addition to the Credit Facility, we have \$25.0 million of uncommitted credit facilities, under which we had no borrowings as of September 27, 2008.

We were in compliance with all debt covenants as of September 27, 2008.

Debt outstanding at September 27, 2008 matures on a calendar year basis as follows:

| <i>In thousands</i>         | <b>2008 Q4</b> | <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012</b> | <b>2013</b> | <b>Thereafter</b> | <b>Total</b> |
|-----------------------------|----------------|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| Contractual debt obligation | \$1,467        | \$135,747   | \$73        | \$6         | \$401,116   | \$200,007   | \$300,022         | \$1,038,438  |

|                  |         |           |      |     |           |           |           |             |
|------------------|---------|-----------|------|-----|-----------|-----------|-----------|-------------|
| maturities       |         |           |      |     |           |           |           |             |
| Other maturities | 156     | 469       |      |     |           |           |           | 625         |
| Total maturities | \$1,623 | \$136,216 | \$73 | \$6 | \$401,116 | \$200,007 | \$300,022 | \$1,039,063 |

On July 8, 2008, we commenced a cash tender offer for all of our outstanding \$250 million aggregate principal 7.85% Senior Notes due 2009 (the Notes). Upon expiration of the tender offer on August 4, 2008, we purchased \$116.1 million aggregate principal amount of the Notes. As a result of this transaction, we recognized a loss of \$4.6 million on early extinguishment of debt. The loss included the write off of \$0.1 million in unamortized deferred financing fees and \$0.6 million in previously unrecognized swap gains, and cash paid of \$5.1 million related to the tender premium and other costs associated with the purchase.

## 12. Derivatives and Financial Instruments

### *Cash-flow hedges*

In August 2007, we entered into a \$105 million interest rate swap agreement with a major financial institution to exchange variable rate interest payment obligations for a fixed rate obligation without the exchange of the underlying principal amounts in order to manage interest rate exposures. The effective date of the swap was August 30, 2007. The swap agreement has a fixed interest rate of 4.89% and expires in May 2012. The fixed interest rate of 4.89% plus the .50% interest rate spread over LIBOR results in an effective fixed interest rate of 5.39%. The fair value of the swap was a liability of \$4.0 million at September 27, 2008 and is recorded in *Other non-current liabilities*.

In September 2005, we entered into a \$100 million interest rate swap agreement with several major financial institutions to exchange variable rate interest payment obligations for fixed rate obligations without the exchange of the underlying principal amounts in order to manage interest rate exposures. The effective date of the fixed rate swap was April 25, 2006. The swap agreement has a fixed interest rate of 4.68% and expires in July 2013.



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The fixed interest rate of 4.68% plus the .60% interest rate spread over LIBOR results in an effective fixed interest rate of 5.28%. The fair value of the swap was a liability of \$3.1 million at September 27, 2008 and is recorded in *Other non-current liabilities*.

The variable to fixed interest rate swaps are designated as and are effective as cash-flow hedges. The fair value of these swaps are recorded as assets or liabilities on the Consolidated Balance Sheets, with changes in their fair value included in *Accumulated other comprehensive income* ( OCI ). Derivative gains and losses included in OCI are reclassified into earnings at the time the related interest expense is recognized or the settlement of the related commitment occurs.

**13. Income Taxes**

The provision for income taxes consists of provisions for federal, state and foreign income taxes. We operate in an international environment with operations in various locations outside the U.S. Accordingly, the consolidated income tax rate is a composite rate reflecting the earnings in the various locations and the applicable rates.

The effective income tax rate for the nine months ended September 27, 2008 was 29.3% compared to 30.5% for the nine months ended September 29, 2007. We expect the effective tax rate for the remainder of 2008 to be between 32% and 33%, resulting in a full year effective income tax rate of between 30.0% and 31.0%. We continue to actively pursue initiatives to reduce our effective tax rate. The tax rate in any quarter can be affected positively or negatively by adjustments that are required to be reported in the specific quarter of resolution.

The total gross liability for uncertain tax positions under FASB Interpretation No. 48 at September 27, 2008 is estimated to be approximately \$25.4 million. We record penalties and interest related to unrecognized tax benefits in *Provision for income taxes* and *Net interest expense*, respectively, which is consistent with our past practices.

**14. Benefit Plans**

Components of net periodic benefit cost for the three and nine months ended September 27, 2008 and September 29, 2007 were as follows:

| <i>In thousands</i>                               | <b>Three months ended</b> |                  |                        |                  |
|---|---------------------------|------------------|------------------------|------------------|
|   | <b>Pension benefits</b>   |                  | <b>Post-retirement</b> |                  |
|   | <b>September</b>          | <b>September</b> | <b>September</b>       | <b>September</b> |
|   | <b>27</b>                 | <b>29</b>        | <b>27</b>              | <b>29</b>        |
|   | <b>2008</b>               | <b>2007</b>      | <b>2008</b>            | <b>2007</b>      |
| Service cost                                      | \$ 3,527                  | \$ 4,331         | \$ 65                  | \$ 146           |
| Interest cost                                     | 8,175                     | 7,891            | 634                    | 746              |
| Expected return on plan assets                    | (7,475)                   | (7,133)          |                        |                  |
| Amortization of transition obligation             | 12                        | 36               |                        |                  |
| Amortization of prior year service cost (benefit) | 45                        | 40               | (34)                   | (62)             |
| Recognized net actuarial loss (gains)             | 68                        | 799              | (825)                  | (355)            |
| Net periodic benefit cost                         | \$ 4,352                  | \$ 5,964         | \$(160)                | \$ 475           |

| <i>In thousands</i> | <b>Nine months ended</b> |                  |                        |                  |
|---------------------|--------------------------|------------------|------------------------|------------------|
|                     | <b>Pension benefits</b>  |                  | <b>Post-retirement</b> |                  |
|                     | <b>September</b>         | <b>September</b> | <b>September</b>       | <b>September</b> |
|                     | <b>27</b>                | <b>29</b>        | <b>27</b>              | <b>29</b>        |
|                     | <b>2008</b>              | <b>2007</b>      | <b>2008</b>            | <b>2007</b>      |
| Service cost        | \$ 10,585                | \$ 12,993        | \$ 195                 | \$ 438           |

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|   |           |           |          |          |
|---|-----------|-----------|----------|----------|
| Interest cost                                     | 24,523    | 23,673    | 1,902    | 2,238    |
| Expected return on plan assets                    | (22,425)  | (21,399)  |          |          |
| Amortization of transition obligation             | 36        | 108       |          |          |
| Amortization of prior year service cost (benefit) | 133       | 120       | (102)    | (186)    |
| Recognized net actuarial loss (gains)             | 204       | 2,395     | (2,475)  | (1,065)  |
| Net periodic benefit cost                         | \$ 13,056 | \$ 17,890 | \$ (480) | \$ 1,425 |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)*****15. Business Segments**

Financial information by reportable segment for the three and nine months ended September 27, 2008 and September 29, 2007 is shown below:

| <i>In thousands</i>                           | <b>Three months ended</b>        |                                  | <b>Nine months ended</b>     |                              |
|---|----------------------------------|----------------------------------|------------------------------|------------------------------|
|   | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> | <b>September 27<br/>2008</b> | <b>September 29<br/>2007</b> |
| <b><i>Net sales to external customers</i></b> |                                  |                                  |                              |                              |
| Water Group                                   | \$566,328                        | \$545,514                        | \$1,726,769                  | \$1,727,925                  |
| Technical Products Group                      | 297,839                          | 275,701                          | 887,559                      | 785,434                      |
| <b>Consolidated</b>                           | <b>\$864,167</b>                 | <b>\$821,215</b>                 | <b>\$2,614,328</b>           | <b>\$2,513,359</b>           |
| <b><i>Intersegment sales</i></b>              |                                  |                                  |                              |                              |
| Water Group                                   | \$ 305                           | \$ 207                           | \$ 816                       | \$ 467                       |
| Technical Products Group                      | 765                              | 1,526                            | 2,937                        | 4,111                        |
| Other   | (1,070)                          | (1,733)                          | (3,753)                      | (4,578)                      |
| <b>Consolidated</b>                           | <b>\$</b>                        | <b>\$</b>                        | <b>\$</b>                    | <b>\$</b>                    |
| <b><i>Operating income (loss)</i></b>         |                                  |                                  |                              |                              |
| Water Group                                   | \$ 47,612                        | \$ 56,061                        | \$ 169,853                   | \$ 207,682                   |
| Technical Products Group                      | 47,585                           | 46,237                           | 142,654                      | 114,008                      |
| Other   | (11,547)                         | (9,148)                          | (37,036)                     | (34,181)                     |
| <b>Consolidated</b>                           | <b>\$ 83,650</b>                 | <b>\$ 93,150</b>                 | <b>\$ 275,471</b>            | <b>\$ 287,509</b>            |

Other sales and operating loss is primarily composed of unallocated corporate expenses, costs related to our captive insurance subsidiary and our intermediate finance companies, and intercompany eliminations.

**16. Warranty**

The changes in the carrying amount of service and product warranties for the nine months ended September 27, 2008 and September 29, 2007 were as follows:

| <i>In thousands</i>                    | <b>September<br/>27<br/>2008</b> | <b>September<br/>29<br/>2007</b> |
|--|----------------------------------|----------------------------------|
| Balance at beginning of the year       | \$ 39,382                        | \$ 34,093                        |
| Service and product warranty provision | 47,910                           | 51,559                           |
| Payments                               | (54,393)                         | (49,476)                         |
| Acquired                               | 184                              | 1,116                            |
| Translation                            | (71)                             | 427                              |

|                              |           |           |
|------------------------------|-----------|-----------|
| Balance at end of the period | \$ 33,012 | \$ 37,719 |
|------------------------------|-----------|-----------|

## 17. Commitments and Contingencies

### *Environmental and Litigation*

There have been no further material developments from the disclosures contained in our 2007 Annual Report on Form 10-K.

### *Horizon Litigation*

The Horizon litigation against our subsidiary Essef Corporation and certain of its subsidiaries by Celebrity Cruise Lines, Inc. ( Celebrity ) was settled by payment of \$35 million to Celebrity in August 2008, a portion of which was covered by insurance. As a result of the settlement, we recorded a charge of \$20.4 million in the second quarter of 2008 which is shown on the line *Legal settlement* in the Condensed Consolidated Statements of Income.

## 18. Financial Statements of Subsidiary Guarantors

The \$133.9 million of Notes due 2009 are jointly and severally guaranteed by 100% owned domestic subsidiaries (the Guarantor Subsidiaries ), each of which is directly or indirectly wholly-owned by Pentair (the Parent Company ). The following supplemental financial information sets forth the condensed consolidated balance sheets as of September 27, 2008, December 31, 2007 and September 29, 2007, the related Condensed Consolidated Statements of Income for the three and nine-months ended September 27, 2008 and September 29, 2007, and Statements of Cash Flows for the nine-months ended September 27, 2008 and September 29, 2007, for the Parent Company, the Guarantor Subsidiaries, the Non-Guarantor Subsidiaries, and total consolidated Pentair and subsidiaries. *Net change in advances to subsidiaries* in the following 2007 Condensed Consolidated Statements of Cash Flows has been reclassified from investing activities to financing activities to conform to the current year presentation. The following condensed financial statements also reflect a change in the presentation of the earnings from investments in subsidiary as previously disclosed in our 2007 footnote.

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Income**  
**For the three months ended September 27, 2008**

| <i>In thousands</i>  | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|---------------------|---------------------|
| Net sales  | \$                        | \$582,577                         | \$ 339,812                            | \$(58,222)          | \$864,167           |
| Cost of goods sold   | 12                        | 422,719                           | 243,973                               | (57,850)            | 608,854             |
| Gross profit   | (12)                      | 159,858                           | 95,839                                | (372)               | 255,313             |
| Selling, general and<br>administrative                     | 21,963                    | 84,430                            | 48,950                                | (371)               | 154,972             |
| Research and development                                   | 117                       | 10,474                            | 6,100                                 |                     | 16,691              |
| Legal settlement   |                           |                                   |                                       |                     |                     |
| Operating (loss) income                                    | (22,092)                  | 64,954                            | 40,789                                | (1)                 | 83,650              |
| Other (income) expense:                                    |                           |                                   |                                       |                     |                     |
| Gain on sale of interest in<br>subsidiaries                |                           |                                   |                                       |                     |                     |
| Earnings from investment in<br>subsidiary                  | (50,645)                  |                                   |                                       | 50,645              |                     |
| Equity losses of unconsolidated<br>subsidiary              |                           | 669                               |                                       |                     | 669                 |
| Loss on early extinguishment of<br>debt                    | 4,611                     |                                   |                                       |                     | 4,611               |
| Net interest (income) expense                              | (22,940)                  | 38,387                            | (1,712)                               |                     | 13,735              |
| Income (loss) before income<br>taxes and minority interest | 46,882                    | 25,898                            | 42,501                                | (50,646)            | 64,635              |
| Provision for income taxes                                 | 5,762                     | 3,184                             | 12,200                                |                     | 21,146              |
| Minority interest  |                           | 2,100                             |                                       |                     | 2,100               |
| Income (loss) from continuing<br>operations                | 41,120                    | 20,614                            | 30,301                                | (50,646)            | 41,389              |
| Loss from discontinued<br>operations, net of tax           |                           | (269)                             |                                       |                     | (269)               |
| Loss on disposal of discontinued<br>operations, net of tax |                           |                                   |                                       |                     |                     |
| Net income (loss)  | \$ 41,120                 | \$ 20,345                         | \$ 30,301                             | \$(50,646)          | \$ 41,120           |

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Income**  
**For the nine months ended September 27, 2008**

**Parent                      Guarantor                      Non-Guarantor**

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| <i>In thousands</i>                                     | <b>Company</b> | <b>Subsidiaries</b> | <b>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|---|----------------|---------------------|---------------------|---------------------|---------------------|
| Net sales   | \$             | \$ 1,914,851        | \$ 880,440          | \$(180,963)         | \$ 2,614,328        |
| Cost of goods sold                                      | 28             | 1,382,979           | 626,854             | (180,239)           | 1,829,622           |
| Gross profit  | (28)           | 531,872             | 253,586             | (724)               | 784,706             |
| Selling, general and administrative                     | 11,761         | 286,659             | 142,233             | (724)               | 439,929             |
| Research and development                                | 283            | 34,141              | 14,447              |                     | 48,871              |
| Legal settlement  |                | 20,435              |                     |                     | 20,435              |
| Operating (loss) income                                 | (12,072)       | 190,637             | 96,906              |                     | 275,471             |
| Other (income) expense:                                 |                |                     |                     |                     |                     |
| Gain on sale of interest in subsidiaries                |                | (109,648)           |                     |                     | (109,648)           |
| Earnings from investment in subsidiary                  | (194,470)      |                     |                     | 194,470             |                     |
| Equity losses of unconsolidated subsidiary              |                | 2,433               |                     |                     | 2,433               |
| Loss on early extinguishment of debt                    | 4,611          |                     |                     |                     | 4,611               |
| Net interest (income) expense                           | (65,062)       | 115,146             | (4,399)             |                     | 45,685              |
| Income (loss) before income taxes and minority interest | 242,849        | 182,706             | 101,305             | (194,470)           | 332,390             |
| Provision for income taxes                              | 18,630         | 49,449              | 29,443              |                     | 97,522              |
| Minority interest                                       |                | 2,100               |                     |                     | 2,100               |
| Income (loss) from continuing operations                | 224,219        | 131,157             | 71,862              | (194,470)           | 232,768             |
| Loss from discontinued operations, net of tax           | (74)           | (8,549)             |                     |                     | (8,623)             |
| Loss on disposal of discontinued operations, net of tax |                |                     |                     |                     |                     |
| Net income (loss)                                       | \$ 224,145     | \$ 122,608          | \$ 71,862           | \$(194,470)         | \$ 224,145          |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Balance Sheets**  
**September 27, 2008**

| <i>In thousands</i>                             | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b>  | <b>Consolidated</b> |
|---|---------------------------|-----------------------------------|---------------------------------------|----------------------|---------------------|
| <b>ASSETS</b>                                   |                           |                                   |                                       |                      |                     |
| <b>Current assets</b>                           |                           |                                   |                                       |                      |                     |
| Cash and cash equivalents                       | \$ 5,288                  | \$ 5,343                          | \$ 82,913                             | \$                   | \$ 93,544           |
| Accounts and notes receivable,<br>net           | 314                       | 349,297                           | 233,419                               | (65,790)             | 517,240             |
| Inventories                                     |                           | 274,238                           | 156,148                               |                      | 430,386             |
| Deferred tax assets                             | 73,336                    | 35,322                            | 7,363                                 | (65,960)             | 50,061              |
| Prepaid expenses and other<br>current assets    | 8,309                     | 13,698                            | 42,434                                | (10,937)             | 53,504              |
| Total current assets                            | 87,247                    | 677,898                           | 522,277                               | (142,687)            | 1,144,735           |
| <b>Property, plant and equipment,<br/>net</b>   | 7,964                     | 179,534                           | 175,854                               |                      | 363,352             |
| <b>Other assets</b>                             |                           |                                   |                                       |                      |                     |
| Investments in/advances to<br>subsidiaries      | 2,405,114                 | 89,990                            | 692,327                               | (3,187,431)          |                     |
| Goodwill  | 2,951                     | 1,333,867                         | 797,213                               |                      | 2,134,031           |
| Intangibles, net                                |                           | 342,374                           | 196,759                               |                      | 539,133             |
| Other   | 72,114                    | 7,719                             | 20,423                                | (30,382)             | 69,874              |
| Total other assets                              | 2,480,179                 | 1,773,950                         | 1,706,722                             | (3,217,813)          | 2,743,038           |
| <b>Total assets</b>                             | <b>\$2,575,390</b>        | <b>\$2,631,382</b>                | <b>\$2,404,853</b>                    | <b>\$(3,360,500)</b> | <b>\$4,251,125</b>  |
| <b>LIABILITIES AND<br/>SHAREHOLDERS EQUITY</b>  |                           |                                   |                                       |                      |                     |
| <b>Current liabilities</b>                      |                           |                                   |                                       |                      |                     |
| Short-term borrowings                           | \$                        | \$                                | \$                                    | \$                   | \$                  |
| Current maturities of long-term<br>debt         | 625                       | 159                               | 239,463                               | (236,334)            | 3,913               |
| Accounts payable                                | 2,333                     | 157,303                           | 131,349                               | (65,057)             | 225,928             |
| Employee compensation and<br>benefits           | 12,711                    | 50,798                            | 43,654                                |                      | 107,163             |
| Current pension and<br>post-retirement benefits | 8,557                     |                                   |                                       |                      | 8,557               |
| Accrued product claims and<br>warranties        |                           | 26,735                            | 16,277                                |                      | 43,012              |

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|   |                    |                    |                    |                      |                    |
|---|--------------------|--------------------|--------------------|----------------------|--------------------|
| Income taxes                                      | (4,053)            | (1,563)            | 13,422             |                      | 7,806              |
| Accrued rebates and sales incentives              |                    | 28,023             | 7,884              |                      | 35,907             |
| Other current liabilities                         | 126,800            | (59,133)           | 44,937             | (10,942)             | 101,662            |
| <b>Total current liabilities</b>                  | <b>146,973</b>     | <b>202,322</b>     | <b>496,986</b>     | <b>(312,333)</b>     | <b>533,948</b>     |
| <b>Other liabilities</b>                          |                    |                    |                    |                      |                    |
| Long-term debt                                    | 1,032,193          | 1,947,540          | 250,824            | (2,195,407)          | 1,035,150          |
| Pension and other retirement compensation         | 73,867             | 17,686             | 73,223             |                      | 164,776            |
| Post-retirement medical and other benefits        | 20,995             | 43,605             |                    | (30,382)             | 34,218             |
| Long-term taxes payable                           | 25,356             |                    |                    |                      | 25,356             |
| Deferred tax liabilities                          | 3,550              | 187,481            | 59,443             | (65,960)             | 184,514            |
| Due to / (from) affiliates                        | (716,943)          | 55,674             | 822,625            | (161,356)            |                    |
| Other non-current liabilities                     | (66,593)           | 108,716            | 54,818             |                      | 96,941             |
| <b>Total liabilities</b>                          | <b>519,398</b>     | <b>2,563,024</b>   | <b>1,757,919</b>   | <b>(2,765,438)</b>   | <b>2,074,903</b>   |
| Minority Interest                                 |                    |                    | 120,230            |                      | 120,230            |
| <b>Shareholders equity</b>                        | <b>2,055,992</b>   | <b>68,358</b>      | <b>526,704</b>     | <b>(595,062)</b>     | <b>2,055,992</b>   |
| <b>Total liabilities and shareholder s equity</b> | <b>\$2,575,390</b> | <b>\$2,631,382</b> | <b>\$2,404,853</b> | <b>\$(3,360,500)</b> | <b>\$4,251,125</b> |



**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Cash Flows**  
**For the nine months ended September 27, 2008**

| <i>In thousands</i>  | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|---------------------|---------------------|
| <b>Operating activities</b>  |                           |                                   |                                       |                     |                     |
| Net income (loss)  | \$ 224,145                | \$ 122,608                        | \$ 71,862                             | \$(194,470)         | \$ 224,145          |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b>           |                           |                                   |                                       |                     |                     |
| (Income) loss from discontinued operations   |                           | 1,217                             |                                       |                     | 1,217               |
| (Gain) loss on disposal of discontinued operations   | 74                        | 7,332                             |                                       |                     | 7,406               |
| Equity losses of unconsolidated subsidiary   |                           | 2,433                             |                                       |                     | 2,433               |
| Minority interest  |                           | (97)                              | 2,197                                 |                     | 2,100               |
| Depreciation   | 898                       | 27,890                            | 16,971                                |                     | 45,759              |
| Amortization   | 1,688                     | 13,275                            | 5,257                                 |                     | 20,220              |
| Earnings from investments in subsidiaries  | (194,470)                 |                                   |                                       | 194,470             |                     |
| Deferred income taxes  | 35                        | 23,839                            | 2,053                                 |                     | 25,927              |
| Stock compensation   | 15,948                    |                                   |                                       |                     | 15,948              |
| Excess tax benefits from stock-based compensation  | (1,617)                   |                                   |                                       |                     | (1,617)             |
| Gain on sale of assets, net  | 87                        |                                   |                                       |                     | 87                  |
| Gain on sale of interest in subsidiaries   |                           | (109,648)                         |                                       |                     | (109,648)           |
| <b>Changes in assets and liabilities, net of effects of business acquisitions and dispositions</b> |                           |                                   |                                       |                     |                     |
| Accounts and notes receivable  | (1,385)                   | (46,364)                          | (22,379)                              | 14,401              | (55,727)            |
| Inventories  |                           | (15,504)                          | (11,014)                              |                     | (26,518)            |
| Prepaid expenses and other current assets  | 25,765                    | (2,970)                           | (26,681)                              | (11,912)            | (15,798)            |
| Accounts payable   | 684                       | (763)                             | 15,823                                | (14,401)            | 1,343               |
| Employee compensation and benefits   | (6,417)                   | (4,763)                           | 3,709                                 |                     | (7,471)             |
| Accrued product claims and warranties  |                           | (5,762)                           | (721)                                 |                     | (6,483)             |
| Income taxes   | (2,655)                   | (1,981)                           | (1,156)                               |                     | (5,792)             |
| Other current liabilities  | (15,746)                  | (8,267)                           | 21,481                                | 11,912              | 9,380               |
| Pension and post-retirement benefits   | 5,031                     | (7,069)                           | 2,630                                 |                     | 592                 |

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|   |           |          |           |           |
|---|-----------|----------|-----------|-----------|
| Other assets and liabilities  | 3,888     | 7,517    | 1,741     | 13,146    |
| Net cash provided by (used for) continuing operations                         | 55,953    | 2,923    | 81,773    | 140,649   |
| Net cash provided by (used for) discontinued operations                       |           | (3,432)  |           | (3,432)   |
| Net cash provided (used for) by operating activities                          | 55,953    | (509)    | 81,773    | 137,217   |
| <b>Investing activities</b>   |           |          |           |           |
| Capital expenditures  | (3,722)   | (25,320) | (11,065)  | (40,107)  |
| Proceeds from sales of property and equipment                                 |           | 177      | 4,127     | 4,304     |
| Acquisitions, net of cash acquired or received                                | (1,627)   |          | 18        | (1,609)   |
| Divestitures  |           | 29,526   |           | 29,526    |
| Other   | (7)       |          |           | (7)       |
| Net cash provided by (used for) investing activities of continuing operations | (5,356)   | 4,383    | (6,920)   | (7,893)   |
| <b>Financing activities</b>   |           |          |           |           |
| Net short-term borrowings (repayments)  | (14,180)  |          |           | (14,180)  |
| Proceeds from long-term debt  | 479,405   |          |           | 479,405   |
| Repayment of long-term debt   | (486,492) |          |           | (486,492) |
| Debt issuance costs   | (114)     |          |           | (114)     |
| Net change in advances to subsidiaries  | 49,585    | (11,126) | (38,459)  |           |
| Excess tax benefit from stock-based compensation                              | 1,617     |          |           | 1,617     |
| Proceeds from exercise of stock options                                       | 5,140     |          |           | 5,140     |
| Repurchases of common stock   | (37,342)  |          |           | (37,342)  |
| Dividends paid  | (43,171)  | 1,123    | (8,493)   | (50,541)  |
| Net cash provided by financing activities of continuing operations            | (45,552)  | (10,003) | (46,952)  | (102,507) |
| <b>Effect of exchange rate changes on cash</b>                                | (6,431)   | 623      | 1,740     | (4,068)   |
| <b>Change in cash and cash equivalents</b>                                    | (1,386)   | (5,506)  | 29,641    | 22,749    |
| <b>Cash and cash equivalents, beginning of period</b>                         | 6,674     | 10,849   | 53,272    | 70,795    |
|   | \$ 5,288  | \$ 5,343 | \$ 82,913 | \$ 93,544 |

**Cash and cash equivalents,  
end of period**

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**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Income**  
**For the three months ended September 29, 2007**

| <i>In thousands</i>  | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|---------------------|---------------------|
| Net sales  | \$                        | \$638,166                         | \$ 234,992                            | \$(51,943)          | \$821,215           |
| Cost of goods sold   |                           | 459,594                           | 168,755                               | (51,830)            | 576,519             |
| Gross profit   |                           | 178,572                           | 66,237                                | (113)               | 244,696             |
| Selling, general and<br>administrative                     | 789                       | 93,016                            | 43,408                                | (113)               | 137,100             |
| Research and development                                   |                           | 10,858                            | 3,588                                 |                     | 14,446              |
| Operating (loss) income                                    | (789)                     | 74,698                            | 19,241                                |                     | 93,150              |
| Other (income) expense:                                    |                           |                                   |                                       |                     |                     |
| Earnings from investment in<br>subsidiary                  | (38,254)                  |                                   |                                       | 38,254              |                     |
| Equity losses of unconsolidated<br>subsidiary              |                           | 845                               |                                       |                     | 845                 |
| Net interest (income) expense                              | (31,874)                  | 50,920                            | (889)                                 |                     | 18,157              |
| Income (loss) before income<br>taxes                       | 69,339                    | 22,933                            | 20,130                                | (38,254)            | 74,148              |
| Provision for income taxes                                 | 11,295                    | 9,168                             | (5,594)                               |                     | 14,869              |
| Income (loss) from continuing<br>operations                | 58,044                    | 13,765                            | 25,724                                | (38,254)            | 59,279              |
| Income from discontinued<br>operations, net of tax         |                           | (1,235)                           |                                       |                     | (1,235)             |
| Gain on disposal of discontinued<br>operations, net of tax |                           |                                   |                                       |                     |                     |
| Net income (loss)  | \$ 58,044                 | \$ 12,530                         | \$ 25,724                             | \$(38,254)          | \$ 58,044           |

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Income**  
**For the nine months ended September 29, 2007**

| <i>In thousands</i> | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|---------------------|---------------------------|-----------------------------------|---------------------------------------|---------------------|---------------------|
| Net sales           | \$                        | \$1,984,338                       | \$ 677,696                            | \$(148,675)         | \$2,513,359         |
| Cost of goods sold  |                           | 1,409,671                         | 491,570                               | (148,058)           | 1,753,183           |
| Gross profit        |                           | 574,667                           | 186,126                               | (617)               | 760,176             |

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|   |            |           |           |             |            |
|---|------------|-----------|-----------|-------------|------------|
| Selling, general and administrative                     | 9,695      | 308,058   | 111,327   | (617)       | 428,463    |
| Research and development                                |            | 33,492    | 10,712    |             | 44,204     |
| Operating (loss) income                                 | (9,695)    | 233,117   | 64,087    |             | 287,509    |
| Other (income) expense:                                 |            |           |           |             |            |
| Earnings from investment in subsidiary                  | (132,229)  |           |           | 132,229     |            |
| Equity losses of unconsolidated subsidiary              |            | 1,838     |           |             | 1,838      |
| Net interest (income) expense                           | (56,289)   | 109,446   | (1,806)   |             | 51,351     |
| Income (loss) before income taxes                       | 178,823    | 121,833   | 65,893    | (132,229)   | 234,320    |
| Provision for income taxes                              | 16,648     | 45,036    | 9,735     |             | 71,419     |
| Income (loss) from continuing operations                | 162,175    | 76,797    | 56,158    | (132,229)   | 162,901    |
| Loss from discontinued operations, net of tax           |            | (726)     |           |             | (726)      |
| Gain on disposal of discontinued operations, net of tax | 207        |           |           |             | 207        |
| Net income (loss)                                       | \$ 162,382 | \$ 76,071 | \$ 56,158 | \$(132,229) | \$ 162,382 |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Balance Sheets**  
**September 29, 2007**

| <i>In thousands</i>                              | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b>  | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|----------------------|---------------------|
| <b>ASSETS</b>                                    |                           |                                   |                                       |                      |                     |
| <b>Current assets</b>                            |                           |                                   |                                       |                      |                     |
| Cash and cash equivalents                        | \$ 5,088                  | \$ 7,068                          | \$ 44,399                             | \$                   | \$ 56,555           |
| Accounts and notes receivable,<br>net            | 279                       | 334,265                           | 191,604                               | (52,652)             | 473,496             |
| Inventories                                      |                           | 269,716                           | 125,922                               |                      | 395,638             |
| Deferred tax assets                              | 98,206                    | 33,193                            | 6,134                                 | (85,495)             | 52,038              |
| Prepaid expenses and other<br>current assets     | 5,446                     | 9,654                             | 48,225                                | (15,579)             | 47,746              |
| Current assets of discontinued<br>operations     |                           | 26,868                            |                                       |                      | 26,868              |
| <b>Total current assets</b>                      | <b>109,019</b>            | <b>680,764</b>                    | <b>416,284</b>                        | <b>(153,726)</b>     | <b>1,052,341</b>    |
| <b>Property, plant and equipment,<br/>net</b>    | <b>5,332</b>              | <b>216,528</b>                    | <b>134,734</b>                        |                      | <b>356,594</b>      |
| <b>Other assets</b>                              |                           |                                   |                                       |                      |                     |
| Investments in/advances to<br>subsidiaries       | 2,431,242                 | 93,623                            | 540,441                               | (3,065,306)          |                     |
| Goodwill   |                           | 1,584,857                         | 404,763                               |                      | 1,989,620           |
| Intangibles, net                                 |                           | 336,924                           | 155,808                               |                      | 492,732             |
| Other  | 72,868                    | 16,157                            | 13,439                                | (25,380)             | 77,084              |
| Non-current assets of<br>discontinued operations |                           | 18,500                            |                                       |                      | 18,500              |
| <b>Total other assets</b>                        | <b>2,504,110</b>          | <b>2,050,061</b>                  | <b>1,114,451</b>                      | <b>(3,090,686)</b>   | <b>2,577,936</b>    |
| <b>Total assets</b>                              | <b>\$2,618,461</b>        | <b>\$2,947,353</b>                | <b>\$1,665,469</b>                    | <b>\$(3,244,412)</b> | <b>\$3,986,871</b>  |
| <b>LIABILITIES AND<br/>SHAREHOLDERS EQUITY</b>   |                           |                                   |                                       |                      |                     |
| <b>Current liabilities</b>                       |                           |                                   |                                       |                      |                     |
| Short-term borrowings                            | \$                        | \$                                | \$ 4,800                              | \$                   | \$ 4,800            |
| Current maturities of long-term<br>debt          | 8,320                     | 156                               | 314,090                               | (317,574)            | 4,992               |
| Accounts payable                                 | (1,559)                   | 154,910                           | 102,051                               | (51,042)             | 204,360             |
| Employee compensation and<br>benefits            | 13,379                    | 55,868                            | 38,024                                |                      | 107,271             |

|  |                    |                    |                    |                      |                    |
|--|--------------------|--------------------|--------------------|----------------------|--------------------|
| Current pension and post-retirement benefits       | 7,918              |                    |                    |                      | 7,918              |
| Accrued product claims and warranties              |                    | 32,739             | 14,980             |                      | 47,719             |
| Income taxes                                       | (6,187)            | 9,322              | 7,727              |                      | 10,862             |
| Accrued rebates and sales incentives               |                    | 29,787             | 7,123              |                      | 36,910             |
| Other current liabilities                          | 27,528             | 51,810             | 48,952             | (16,457)             | 111,833            |
| Current liabilities of discontinued operations     |                    | 5,431              |                    |                      | 5,431              |
| <b>Total current liabilities</b>                   | <b>49,399</b>      | <b>340,023</b>     | <b>537,747</b>     | <b>(385,073)</b>     | <b>542,096</b>     |
| <b>Other liabilities</b>                           |                    |                    |                    |                      |                    |
| Long-term debt                                     | 1,071,549          | 1,972,692          | 46,124             | (1,987,658)          | 1,102,707          |
| Pension and other retirement compensation          | 125,909            | 28,848             | 67,341             |                      | 222,098            |
| Post-retirement medical and other benefits         | 22,268             | 49,611             |                    | (25,380)             | 46,499             |
| Long-term taxes payable                            | 18,214             |                    |                    |                      | 18,214             |
| Deferred tax liabilities                           | 3,232              | 159,157            | 57,789             | (85,495)             | 134,683            |
| Due to / (from) affiliates                         | (532,170)          | 257,329            | 670,822            | (395,981)            |                    |
| Other non-current liabilities                      | 31,903             | 7,362              | 50,633             |                      | 89,898             |
| Non-current liabilities of discontinued operations |                    | 2,519              |                    |                      | 2,519              |
| <b>Total liabilities</b>                           | <b>790,304</b>     | <b>2,817,541</b>   | <b>1,430,456</b>   | <b>(2,879,587)</b>   | <b>2,158,714</b>   |
| <b>Shareholders equity</b>                         | <b>1,828,157</b>   | <b>129,812</b>     | <b>235,013</b>     | <b>(364,825)</b>     | <b>1,828,157</b>   |
| <b>Total liabilities and shareholders equity</b>   | <b>\$2,618,461</b> | <b>\$2,947,353</b> | <b>\$1,665,469</b> | <b>\$(3,244,412)</b> | <b>\$3,986,871</b> |

**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Cash Flows**  
**For the nine months ended September 29, 2007**

| <i>In thousands</i>  | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|---------------------|---------------------|
| <b>Operating activities</b>  |                           |                                   |                                       |                     |                     |
| Net income (loss)  | \$ 162,382                | \$ 76,071                         | \$ 56,158                             | \$(132,229)         | \$ 162,382          |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b>           |                           |                                   |                                       |                     |                     |
| (Income) loss from discontinued operations   |                           | 726                               |                                       |                     | 726                 |
| (Gain) loss on disposal of discontinued operations   | (207)                     |                                   |                                       |                     | (207)               |
| Equity losses of unconsolidated subsidiary   |                           | 1,838                             |                                       |                     | 1,838               |
| Depreciation   | 900                       | 30,191                            | 14,447                                |                     | 45,538              |
| Amortization   | 3,250                     | 11,774                            | 3,611                                 |                     | 18,635              |
| Earnings from investments in subsidiaries  | (132,229)                 |                                   |                                       | 132,229             |                     |
| Deferred income taxes  | (1,007)                   |                                   | (17,876)                              |                     | (18,883)            |
| Stock compensation   | 17,071                    |                                   |                                       |                     | 17,071              |
| Excess tax benefits from stock-based compensation  | (2,706)                   |                                   |                                       |                     | (2,706)             |
| Intercompany Dividends   | (23)                      | 13,714                            | (13,691)                              |                     |                     |
| Gain on sale of assets, net  | (2,195)                   |                                   |                                       |                     | (2,195)             |
| Gain on sale of interest in subsidiaries   |                           |                                   |                                       |                     |                     |
| <b>Changes in assets and liabilities, net of effects of business acquisitions and dispositions</b> |                           |                                   |                                       |                     |                     |
| Accounts and notes receivable  | 6,468                     | (13,873)                          | (28,858)                              | 8,336               | (27,927)            |
| Inventories  |                           | 8,695                             | 5,278                                 |                     | 13,973              |
| Prepaid expenses and other current assets  | 7,022                     | 13,500                            | (29,262)                              | 59                  | (8,681)             |
| Accounts payable   | (4,419)                   | (1,089)                           | 12,749                                | (8,329)             | (1,088)             |
| Employee compensation and benefits   | (4,670)                   | 6,956                             | 751                                   |                     | 3,037               |
| Accrued product claims and warranties  |                           | 3,783                             | (584)                                 |                     | 3,199               |
| Income taxes   | (5,063)                   | 342                               | 148                                   |                     | (4,573)             |
| Other current liabilities  | 9,957                     | (8,869)                           | 14,929                                | (62)                | 15,955              |
| Pension and post-retirement benefits   | 3,354                     | 910                               | 3,660                                 |                     | 7,924               |



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|   |           |           |           |     |           |
|---|-----------|-----------|-----------|-----|-----------|
| Other assets and liabilities  | 2,537     | 763       | 4,096     |     | 7,396     |
| Net cash provided by (used for) continuing operations                         | 60,422    | 145,432   | 25,556    | 4   | 231,414   |
| Net cash provided by (used for) discontinued operations                       | (207)     | (2,081)   | 207       |     | (2,081)   |
| Net cash provided by (used for) operating activities                          | 60,215    | 143,351   | 25,763    | 4   | 229,333   |
| <b>Investing activities</b>   |           |           |           |     |           |
| Capital expenditures  | (1,480)   | (23,317)  | (20,366)  |     | (45,163)  |
| Proceeds from sales of property and equipment                                 |           | 951       | 4,185     |     | 5,136     |
| Acquisitions, net of cash acquired or received                                | (485,913) |           | (351)     |     | (486,264) |
| Other   | (606)     | (3,438)   |           |     | (4,044)   |
| Net cash provided by (used for) investing activities of continuing operations | (487,999) | (25,804)  | (16,532)  |     | (530,335) |
| <b>Financing activities</b>   |           |           |           |     |           |
| Net short-term borrowings (repayments)  |           |           | (10,378)  |     | (10,378)  |
| Proceeds from long-term debt  | 1,147,132 |           |           |     | 1,147,132 |
| Repayment of long-term debt   | (770,822) |           |           |     | (770,822) |
| Debt issuance costs   | (1,876)   |           |           |     | (1,876)   |
| Net change in advances to subsidiaries  | 98,009    | (119,310) | 21,305    | (4) |           |
| Excess tax benefit from stock-based compensation                              | 2,706     |           |           |     | 2,706     |
| Proceeds from exercise of stock options                                       | 5,512     |           |           |     | 5,512     |
| Repurchases of common stock   | (27,119)  |           |           |     | (27,119)  |
| Dividends paid  | (44,986)  |           |           |     | (44,986)  |
| Net cash provided by (used for) financing activities of continuing operations | 408,556   | (119,310) | 10,927    | (4) | 300,169   |
| <b>Effect of exchange rate changes on cash</b>                                | 15,506    | 2,281     | (15,219)  |     | 2,568     |
| <b>Change in cash and cash equivalents</b>                                    | (3,722)   | 518       | 4,939     |     | 1,735     |
| <b>Cash and cash equivalents, beginning of period</b>                         | 8,810     | 6,550     | 39,460    |     | 54,820    |
| <b>Cash and cash equivalents, end of period</b>                               | \$ 5,088  | \$ 7,068  | \$ 44,399 | \$  | \$ 56,555 |



**Table of Contents*****Pentair, Inc. and subsidiaries******Notes to condensed consolidated financial statements (unaudited)***

**Pentair, Inc. and Subsidiaries**  
**Unaudited Condensed Consolidated Balance Sheets**  
**December 31, 2007**

| <i>In thousands</i>                              | <b>Parent<br/>Company</b> | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Eliminations</b>  | <b>Consolidated</b> |
|--|---------------------------|-----------------------------------|---------------------------------------|----------------------|---------------------|
| <b>ASSETS</b>                                    |                           |                                   |                                       |                      |                     |
| <b>Current assets</b>                            |                           |                                   |                                       |                      |                     |
| Cash and cash equivalents                        | \$ 6,674                  | \$ 10,849                         | \$ 53,272                             | \$                   | \$ 70,795           |
| Accounts and notes receivable,<br>net            | 522                       | 329,230                           | 188,313                               | (51,390)             | 466,675             |
| Inventories                                      |                           | 267,742                           | 124,674                               |                      | 392,416             |
| Deferred tax assets                              | 70,494                    | 35,152                            | 7,947                                 | (63,082)             | 50,511              |
| Prepaid expenses and other<br>current assets     | 12,673                    | 9,392                             | 37,246                                | (23,403)             | 35,908              |
| Current assets of discontinued<br>operations     |                           | 21,716                            |                                       |                      | 21,716              |
| <b>Total current assets</b>                      | <b>90,363</b>             | <b>674,081</b>                    | <b>411,452</b>                        | <b>(137,875)</b>     | <b>1,038,021</b>    |
| <b>Property, plant and equipment,<br/>net</b>    | <b>5,140</b>              | <b>218,989</b>                    | <b>141,861</b>                        |                      | <b>365,990</b>      |
| <b>Other assets</b>                              |                           |                                   |                                       |                      |                     |
| Investments in/advances to<br>subsidiaries       | 2,434,205                 | 90,212                            | 575,238                               | (3,099,655)          |                     |
| Goodwill   |                           | 1,587,996                         | 416,724                               |                      | 2,004,720           |
| Intangibles, net                                 |                           | 329,056                           | 162,207                               |                      | 491,263             |
| Other  | 80,575                    | 14,990                            | 17,054                                | (30,382)             | 82,237              |
| Non-current assets of<br>discontinued operations |                           | 18,383                            |                                       |                      | 18,383              |
| <b>Total other assets</b>                        | <b>2,514,780</b>          | <b>2,040,637</b>                  | <b>1,171,223</b>                      | <b>(3,130,037)</b>   | <b>2,596,603</b>    |
| <b>Total assets</b>                              | <b>\$2,610,283</b>        | <b>\$2,933,707</b>                | <b>\$1,724,536</b>                    | <b>\$(3,267,912)</b> | <b>\$4,000,614</b>  |
| <b>LIABILITIES AND<br/>SHAREHOLDERS EQUITY</b>   |                           |                                   |                                       |                      |                     |
| <b>Current liabilities</b>                       |                           |                                   |                                       |                      |                     |
| Short-term borrowings                            | \$                        | \$                                | \$ 13,586                             | \$                   | \$ 13,586           |
| Current maturities of long-term<br>debt          | 20,114                    | 158                               | 338,827                               | (354,024)            | 5,075               |
| Accounts payable                                 | 2,138                     | 174,672                           | 104,336                               | (51,209)             | 229,937             |
| Employee compensation and<br>benefits            | 15,935                    | 58,790                            | 36,750                                |                      | 111,475             |

|  |                    |                    |                    |                      |                    |
|--|--------------------|--------------------|--------------------|----------------------|--------------------|
| Current pension and post-retirement benefits       | 8,557              |                    |                    |                      | 8,557              |
| Accrued product claims and warranties              |                    | 34,378             | 15,004             |                      | 49,382             |
| Income taxes                                       | 3,207              | (5,628)            | 15,340             |                      | 12,919             |
| Accrued rebates and sales incentives               |                    | 28,209             | 8,454              |                      | 36,663             |
| Other current liabilities                          | 19,510             | 52,940             | 40,779             | (22,852)             | 90,377             |
| Current liabilities of discontinued operations     |                    | 2,935              |                    |                      | 2,935              |
| <b>Total current liabilities</b>                   | <b>69,461</b>      | <b>346,454</b>     | <b>573,076</b>     | <b>(428,085)</b>     | <b>560,906</b>     |
| <b>Other liabilities</b>                           |                    |                    |                    |                      |                    |
| Long-term debt                                     | 1,021,464          | 1,972,655          | 34,139             | (1,986,333)          | 1,041,925          |
| Pension and other retirement compensation          | 67,872             | 22,905             | 70,265             |                      | 161,042            |
| Post-retirement medical and other benefits         | 21,958             | 45,571             |                    | (30,382)             | 37,147             |
| Long-term taxes payable                            | 21,306             |                    |                    |                      | 21,306             |
| Deferred tax liabilities                           | 3,429              | 168,815            | 58,471             | (63,082)             | 167,633            |
| Due to / (from) affiliates                         | (542,763)          | 205,731            | 689,149            | (352,117)            |                    |
| Other non-current liabilities                      | 36,685             | 7,085              | 53,316             |                      | 97,086             |
| Non-current liabilities of discontinued operations |                    | 2,698              |                    |                      | 2,698              |
| <b>Total liabilities</b>                           | <b>699,412</b>     | <b>2,771,914</b>   | <b>1,478,416</b>   | <b>(2,859,999)</b>   | <b>2,089,743</b>   |
| <b>Shareholders equity</b>                         | <b>1,910,871</b>   | <b>161,793</b>     | <b>246,120</b>     | <b>(407,913)</b>     | <b>1,910,871</b>   |
| <b>Total liabilities and shareholders equity</b>   | <b>\$2,610,283</b> | <b>\$2,933,707</b> | <b>\$1,724,536</b> | <b>\$(3,267,912)</b> | <b>\$4,000,614</b> |

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

This report contains statements that we believe to be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements give our current expectations or forecasts of future events. Forward-looking statements generally can be identified by the use of forward-looking terminology such as may, will, expect, intend, estimate, anticipate, believe, project, or continue, or the negative thereof. From time to time, we also may provide oral or written forward-looking statements in other materials we release to the public. Any or all of our forward-looking statements in this report and in any public statements we make could be materially different from actual results. They can be affected by assumptions we might make or by known or unknown risks or uncertainties. Consequently, we cannot guarantee any forward-looking statements. Investors are cautioned not to place undue reliance on any forward-looking statements. Investors should also understand that it is not possible to predict or identify all such factors and should not consider the following list to be a complete statement of all potential risks and uncertainties.

The following factors and those discussed in ITEM 1A, Risk Factors, included in our 2007 Annual Report on Form 10-K may impact the achievement of forward-looking statements:

- § general economic and political conditions, such as political instability, credit market uncertainty, the rate of economic growth or decline in our principal geographic or product markets or fluctuations in exchange rates;

changes in general economic and industry conditions in markets in which we participate, such as:

- § continued deterioration in the North American housing market;
  - § the strength of product demand and the markets we serve;
  - § the intensity of competition, including that from foreign competitors;
  - § pricing pressures;
  - § the financial condition of our customers;
  - § market acceptance of new product introductions and enhancements;
  - § the introduction of new products and enhancements by competitors;
  - § our ability to maintain and expand relationships with large customers;
  - § our ability to source raw material commodities from our suppliers without interruption and at reasonable prices; and
  - § our ability to source components from third parties, in particular from foreign manufacturers, without interruption and at reasonable prices;
- our ability to access capital markets and obtain anticipated financing under favorable terms;

our ability to identify, complete and integrate acquisitions successfully and to realize expected synergies on our anticipated timetable;

changes in our business strategies, including acquisition, divestiture and restructuring activities;

domestic and foreign governmental and regulatory policies;

changes in operating factors, such as continued improvement in manufacturing activities and the achievement of related efficiencies, cost reductions and inventory risks due to shifts in market demand and costs associated with moving production overseas;

our ability to generate savings from our excellence in operations initiatives consisting of lean enterprise, supply management and cash flow practices;

our ability to generate savings from our restructuring actions;

unanticipated developments that could occur with respect to contingencies such as litigation, intellectual property matters, product liability exposures and environmental matters; and

our ability to accurately evaluate the effects of contingent liabilities such as tax, product liability, environmental and other claims.

The foregoing factors are not exhaustive, and new factors may emerge or changes to the foregoing factors may occur that would impact our business. We assume no obligation, and disclaim any duty, to update the forward-looking statements in this report.

### **Overview**

We are a focused diversified industrial manufacturing company comprised of two operating segments: Water and Technical Products. Our Water Group is a global leader in providing innovative products and systems used worldwide in the movement, storage, treatment and enjoyment of water. Our Technical Products Group is a leader in the global enclosures and thermal management markets, designing and manufacturing standard, modified and custom enclosures, which that house and protect sensitive electronics and electrical components, thermal management products and accessories. In 2008, we expect our Water Group and Technical Products Group to generate approximately 2/3 and 1/3 of total revenues, respectively.

Our Water Group has progressively become a more important part of our business portfolio with sales increasing from approximately \$125 million in 1995 to approximately \$2.3 billion in 2007. We believe the water industry is structurally attractive as a result of a growing demand for clean water and the large global market size (of which we have identified a target market totaling \$60 billion). Our vision is to be a leading global provider of innovative products and systems used in the movement, storage, treatment and enjoyment of water.

On February 29, 2008, we sold our National Pool Tile ( NPT ) business to Pool Corporation in a cash transaction for approximately \$30.0 million subject to certain price adjustments. The results of NPT have been reported as discontinued operations for all periods presented. The assets and liabilities of NPT have been reclassified as discontinued operations for all periods presented.

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On June 28, 2008, we entered into a transaction with GE Water & Process Technologies (a unit of General Electric Company) ( GE ) that was accounted for as an acquisition of an 80.1 percent ownership interest in GE s global water softener and residential water filtration business in exchange for a 19.9 percent interest in our global water softener and residential water filtration business (the GE Transaction ). The acquisition was effected through the formation of two new entities, a U.S. entity and an international entity, into which we and GE contributed certain assets, properties, liabilities and operations representing their respective global water softener and residential water filtration businesses. We are an 80.1 percent owner of the new entities and GE is a 19.9 percent owner.

Our Technical Products Group operates in a large global market with significant potential for growth in industry segments such as defense, security, medical and networking. We believe we have the largest industrial and commercial distribution network in North America for enclosures and the highest brand recognition in the industry in North America. From mid-2001 through 2003, the Technical Products Group experienced significantly lower sales volumes as a result of severely reduced capital spending in the industrial and commercial markets and over-capacity and weak demand in the datacommunication and telecommunication markets. From 2004 through 2008, sales volumes increased due to the addition of new distributors, new products and higher demand in targeted markets.

### ***Key Trends and Uncertainties***

The following trends and uncertainties affected the first nine months of our financial performance through 2008 and will likely impact our results in the future:

We believe many markets we serve are slowing as a result of the tumultuous credit markets and the consequent anticipated general unfavorable economic impact around the world. We have identified specific applications and geographic markets we believe will stagnate, contract or continue contracting over the next two years. We have begun and expect to continue to restructure our operations serving those markets to reduce capacity and costs, optimize our manufacturing footprint and simplify our infrastructure. We have also identified specific markets in which we participate that we believe will continue to grow over this period and are selectively reinforcing our businesses in these markets.

The housing market and new pool starts slowed in 2006 and 2007, and shrank significantly in the first nine months of 2008. We believe that construction of new homes and new pool starts in North America affect approximately 10% - 15% of sales of our water businesses. We expect this downturn to adversely impact our sales for the remainder of 2008 and may continue to affect sales in 2009. As sales of products into domestic residential end-markets in our Water Group business continued to slow appreciably, we have reduced our investments in businesses in those markets, and further restructured our operations by closing or downsizing facilities, reducing headcount and taking other market-related actions.

The telecommunication equipment market, particularly in North America, slowed throughout 2007 and impacted North American electronics sales within our Technical Products Group. The 2007 revenue decrease was attributable to telecommunication industry consolidation (which has delayed enclosure product sales) and some Original Equipment Manufacturer ( OEM ) datacommunication programs reaching end-of-life. Based on some recovery of telecommunication equipment procurement in the second half of 2007 and the first nine months of 2008, we anticipate continuing improvement in the remainder of 2008 and an annual growth rate in the high single digits for our North American electronics sales. A weak economy in the United States and Europe would likely reduce marketplace spending on telecommunication capital investments and therefore our anticipated revenue growth.

We experienced year over year favorable foreign currency effects on net sales and operating results in 2007 and the first nine months of 2008, due to the weakening of the U.S. dollar in relation to other foreign currencies. Our currency effect is primarily for the U.S. dollar against the euro, which strengthened in late September and early October 2008, and which may or may not trend favorably in the future.

We are experiencing material cost and other inflation in a number of our businesses. We are striving for greater productivity improvements and implementing selective increases in selling prices to help mitigate cost increases we have experienced in base materials such as carbon steel, copper and resins and other costs such as health care and other employee benefit costs.

We expect our operations to continue to benefit from our Pentair Integrated Management System ( PIMS ) initiatives, which include strategy deployment; lean enterprise with special focus on sourcing and supply management, cash flow management and lean operations; and IGNITE, our process to drive organic growth.

We have a long-term goal to consistently generate free cash flow that equals or exceeds 100% conversion of our adjusted net income. We define free cash flow as cash flow from continuing operating activities less capital expenditures plus proceeds from sale of property and equipment. Free cash flow for the full year 2007 was approximately \$285 million, or 135% of our net income. See our discussion of *Other financial measures* under the caption *Liquidity and Capital Resources* in this report.

We experience seasonal demand in a number of markets within our Water Group. End-user demand for pool equipment follows warm weather trends and is normally at seasonal highs from April to August. The magnitude of the sales spike is partially mitigated by employing some advance sale early buy programs (generally including extended payment terms and/or additional discounts). Demand for residential and agricultural water systems is also impacted by economic conditions and weather patterns, particularly by heavy flooding and droughts.

On June 28, 2008, we completed the GE Transaction. We believe this transaction provides us with expanded revenue growth and cost synergy opportunities. The one-time gain on the transaction increased diluted earnings per share, on an after tax basis, by 86 cents in the second quarter of 2008.



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The effective income tax rate for the nine months ended September 27, 2008 was 29.3% compared to 30.5% for the nine months ended September 29, 2007. We expect the effective tax rate for the remainder of 2008 to be between 32% and 33%, resulting in a full year effective income tax rate of between 30.0% and 31.0%. We continue to actively pursue initiatives to reduce our effective tax rate. The tax rate in any quarter can be affected positively or negatively by adjustments that are required to be reported in the specific quarter of resolution.

**Outlook**

In 2008, our operating objectives include the following:

Restructuring our operations in challenging markets while investing in higher growth markets and geographies;

Increasing our vertical market focus within each of our Global Business Units to grow in those markets in which we have competitive advantages;

Driving operating excellence through lean enterprise initiatives, with special focus on sourcing and supply management, cash flow management, and lean operations;

Stressing proactive talent development, particularly in international management and other key functional areas; and

Completing integration of prior acquisitions and realizing identified synergistic opportunities.

On October 21, 2008, we updated our fiscal 2008 earnings guidance to approximately \$2.51 to \$2.54 per share on a reported generally accepted accounting principles ( GAAP ) basis. In the fourth quarter, we anticipate earnings per share to be approximately \$0.17 \$0.20, taking into account approximately \$0.35 per share in changes for restructuring actions to position our operations for increasingly difficult markets.

Our outlook for the fourth quarter is based on several variables. First, we anticipate modest revenue growth in the low single digits, bringing our total revenue to approximately \$3.5 billion for the full year. Second, we expect to get the benefit of restructuring and other market-related expense reduction efforts taken in the second and third quarters of 2008. Third, we will have certain integration costs and intangible amortization charges incurred in connection with the GE Transaction. Fourth, as noted above, we will be adversely impacted by the expenses and charges associated with the additional cost reduction actions announced in the fourth quarter of 2008.

Our guidance assumes an absence of significant acquisitions or divestitures in 2008, other than the GE Transaction. As noted above, in 2008 we may seek to expand our geographic reach internationally, expand our presence in our various channels to market and acquire technologies and products to broaden our businesses capabilities to serve additional markets. We may also consider the divestiture or closure of discrete business units to further focus our businesses on their most attractive markets.

The Company has not yet introduced guidance for fiscal year 2009, due to the heightened uncertainty around the globe in those markets in which we participate. We anticipate publishing fiscal year 2009 guidance in December.

The ability to achieve our operating objectives will depend, to a certain extent, on factors outside our control. See

Forward-looking statements in this report and Risk Factors under ITEM 1A in our 2007 Annual Report on Form 10-K.

**RESULTS OF OPERATIONS****Net sales**

Consolidated net sales and the change from the prior year period were as follows:

|                     | Three months ended |                 |           |        | Nine months ended |                 |           |        |
|---------------------|--------------------|-----------------|-----------|--------|-------------------|-----------------|-----------|--------|
|                     | September<br>27    | September<br>29 |           | %      | September<br>27   | September<br>29 |           | %      |
| <i>In thousands</i> | 2008               | 2007            | \$ change | change | 2008              | 2007            | \$ change | change |
| Net sales           | \$864,167          | \$821,215       | \$42,952  | 5.2%   | \$2,614,328       | \$2,513,359     | \$100,969 | 4.0%   |

*The components of the net sales change in 2008 from 2007 were as follows:*

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| <i>Percentages</i> | <b>% Change from 2007</b> |                    |
|--------------------|---------------------------|--------------------|
|                    | <b>Three months</b>       | <b>Nine months</b> |
| Volume             | 0.8                       | (0.6)              |
| Price              | 2.4                       | 1.9                |
| Currency           | 2.0                       | 2.7                |
| Total              | 5.2                       | 4.0                |

*Consolidated net sales*

The 5.2 percent and 4.0 percent increases in consolidated net sales in the third quarter and first nine months, respectively, of 2008 from 2007 were primarily driven by:

favorable foreign currency effects;

an increase in sales volume due to the GE Transaction and our April 30, 2007 acquisition of Porous Media Corporation and Porous Media, Ltd. (together "Porous Media");

selective increases in selling prices to mitigate inflationary cost increases; and

higher Technical Products Group sales into electrical markets.

These increases were partially offset by:

lower sales of certain pump, pool and filtration products primarily related to the downturn in the North American residential housing market.

Net sales by segment and the change from the prior year period were as follows:

| <i>In thousands</i> | <b>Three months ended</b> |                  |                  |                 | <b>Nine months ended</b> |                  |                  |                 |
|---------------------|---------------------------|------------------|------------------|-----------------|--------------------------|------------------|------------------|-----------------|
|                     | <b>September</b>          | <b>September</b> | <b>\$ change</b> | <b>% change</b> | <b>September</b>         | <b>September</b> | <b>\$ change</b> | <b>% change</b> |
|                     | <b>27</b>                 | <b>27</b>        |                  |                 | <b>27</b>                | <b>27</b>        |                  |                 |
| Water               | \$566,328                 | \$545,514        | \$20,814         | 3.8%            | \$1,726,769              | \$1,727,925      | \$ (1,156)       | (0.1%)          |
| Technical Products  | 297,839                   | 275,701          | 22,138           | 8.0%            | 887,559                  | 785,434          | 102,125          | 13.0%           |
| Total               | \$864,167                 | \$821,215        | \$42,952         | 5.2%            | \$2,614,328              | \$2,513,359      | \$100,969        | 4.0%            |

**Water**

The 3.8 percentage point increase in the Water Group net sales in the third quarter of 2008 from 2007 was primarily driven by:

an increase in sales volume driven by the GE Transaction;

selective increases in selling prices to mitigate inflationary cost increases;

increased sales into the global commercial, municipal and agricultural markets;

continued growth in China and in other markets in Asia-Pacific as well as continued success in penetrating markets in Eastern Europe and the Middle East; and

favorable foreign currency effects.

These increases were offset by:

organic sales decline of 1.4 percent for the third quarter of 2008 (excluding acquisitions and foreign currency exchange), which included lower sales of certain pump, pool and filtration products primarily related to the downturn in the North American residential housing market and the slowing of residential markets in Western Europe.

*The 0.1 percentage point decrease in the Water Group net sales in first nine months of 2008 from 2007 was primarily driven by:*

organic sales decline of 5.1 percent for the first nine months of 2008 (excluding acquisitions and foreign currency exchange), which included:

- § lower sales of certain pump, pool and filtration products primarily related to the downturn in the North American residential housing market; and
  
- § second quarter 2007 sales of municipal pumps related to a large flood control project, which did not recur in 2008.

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*These decreases were partially offset by:*

§ selective increases in selling prices to mitigate inflationary cost increases; and

§ continued growth in China and in other markets in Asia-Pacific as well as continued success in penetrating markets in Eastern Europe and the Middle East.

These decreases were further offset by:

an increase in sales volume driven by our February 2, 2007 acquisition of Jung Pumpen GmbH ( Jung Pump ), our April 30, 2007 acquisition of Porous Media and the GE Transaction; and

favorable foreign currency effects.

**Technical Products**

*The 8.0 percent and 13.0 percent increase in Technical Products Group net sales in the third quarter and first nine months, respectively, of 2008 from 2007 were primarily driven by:*

an increase in sales into electrical markets, which includes new products and selective increases in selling prices to mitigate inflationary cost increases;

favorable foreign currency effects;

strong sales performance in Asia and Europe; and

an increase in sales into electronics markets as orders and sales to our telecommunications customers rebounded and we continued to expand into other vertical markets.

These increases were partially offset by:

decreases in sales into North American electronics markets.

**Gross profit**

|                         | Three months ended      |               |                         |               | Nine months ended       |               |                         |               |
|-------------------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|
|                         | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales |
| <i>In thousands</i>     |                         |               |                         |               |                         |               |                         |               |
| Gross profit            | \$255,313               | 29.5%         | \$244,696               | 29.8%         | \$784,706               | 30.0%         | \$760,176               | 30.2%         |
| Percentage point change |                         | (0.3) pts     |                         |               |                         | (0.2) pts     |                         |               |

*The 0.3 percent and 0.2 percent decreases in gross profit as a percentage of sales in the third quarter and first nine months, respectively, of 2008 from 2007 were primarily the result of:*

inflationary increases related to raw materials and labor;

lower sales of certain pump, pool and filtration products primarily related to the downturn in the North American residential housing market and the slowing of residential markets in Western Europe; and

higher cost of goods sold in 2008 as a result of a fair market value inventory step-up related to the GE Transaction.

*These decreases were partially offset by:*

the gross margin impact from higher Technical Products Group sales and the resulting improved fixed cost leverage;

selective increases in selling prices in our Water and Technical Products Groups to mitigate inflationary cost increases;

savings generated from our PIMS initiatives including lean and supply management practices; and

lower comparative cost in 2008 for our Jung Pump and Porous Media businesses due to the absence of a fair market value inventory step-up that was recorded in connection with those acquisitions.

**Table of Contents****\*Selling, general and administrative (SG&A)**

| <i>In thousands</i>        | Three months ended      |               | September               |               | September               |               | September               |               |
|----------------------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|
|                            | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales |
| *SG&A                      | \$154,972               | 17.9%         | \$137,100               | 16.7%         | \$460,364               | 17.6%         | \$428,463               | 17.0%         |
| Percentage point<br>change |                         | 1.2 pts       |                         |               |                         | 0.6 pts       |                         |               |

\* Includes Legal settlement

The 1.2 percentage point increase in SG&A expense as a percentage of sales in the third quarter of 2008 from 2007 was primarily due to:

restructuring actions primarily in our Water Group during the third quarter of 2008; and

higher selling, general and administrative expenses to fund investments in future growth with emphasis on growth in the international markets, including personnel and business infrastructure investments.

These increases were partially offset by:

reduced costs related to productivity actions taken in the second half of 2007; and

reduced costs related to the completion of the European SAP implementation in 2007.

The 0.6 percentage point increase in SG&A expense as a percentage of sales in the first nine months of 2008 from 2007 was primarily due to:

expenses in the second quarter related to the settlement of the Horizon litigation;

restructuring actions primarily in our Water Group taken during the second and third quarters of 2008; and

higher selling, general and administrative expenses to fund investments in future growth with emphasis on growth in the international markets, including personnel and business infrastructure investments.

These increases were partially offset by:

reduced costs related to productivity actions taken in the second half of 2007; and

reduced costs related to the completion of the European SAP implementation in 2007.

**Research and development (R&D)**

| <i>In thousands</i>        | Three months ended      |               | September               |               | September               |               | September               |               |
|----------------------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|
|                            | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales |
| R&D                        | \$16,691                | 1.9%          | \$14,446                | 1.8%          | \$48,871                | 1.9%          | \$44,204                | 1.8%          |
| Percentage point<br>change |                         | 0.1 pts       |                         |               |                         | 0.1 pts       |                         |               |

The 0.1 percentage point increase as a percentage of sales in the third quarter 2008 from 2007 and the first nine months of 2008 from 2007 were primarily due to:

increased R&D expense spending with emphasis on new product development and value engineering.

**Operating income**  
**Water**

| <i>In thousands</i>        | Three months ended      |               | September               |               | September               |               | Nine months ended       |               |
|----------------------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|
|                            | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales |
| Operating<br>income        | \$47,612                | 8.4%          | \$56,061                | 10.3%         | \$169,853               | 9.8%          | \$207,682               | 12.0%         |
| Percentage point<br>change |                         | (1.9) pts     |                         |               |                         |               | (2.2) pts               |               |

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*The 1.9 and 2.2 percentage point decreases in Water Group operating income as a percentage of sales in the third quarter and first nine months, respectively, of 2008 from 2007 were primarily the result of:*

inflationary increases related to raw materials and labor;

a decline in sales of certain pump, pool and filtration products resulting from the downturn in the North American residential housing markets;

expenses in the second quarter related to the settlement of the Horizon litigation;

restructuring actions taken during the second and third quarters of 2008;

second quarter 2007 sales of municipal pumps related to a large flood control project, which did not recur in 2008; and

higher cost in 2008 as a result of a fair market value inventory step-up and intangible amortization related to the June 2008 GE Transaction.

*These decreases were partially offset by:*

selective increases in selling prices to mitigate inflationary cost increases;

savings generated from our PIMS initiatives, including lean and supply management practices;

an increase in sales volume driven by our February 2, 2007 acquisition of Jung Pump, our April 30, 2007 acquisition of Porous Media and the GE Transaction; and

lower comparative cost in 2008 for our Jung and Porous Media businesses due to the absence of a fair market value inventory step-up that was recorded in connection with those acquisitions.

**Technical Products**

|                     | Three months ended      |               |                         |               | Nine months ended       |               |                         |               |
|---------------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|-------------------------|---------------|
|                     | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales | September<br>27<br>2008 | % of<br>sales | September<br>29<br>2007 | % of<br>sales |
| <i>In thousands</i> |                         |               |                         |               |                         |               |                         |               |
| Operating income    | \$47,585                | 16.0%         | \$46,237                | 16.8%         | \$142,654               | 16.1%         | \$114,008               | 14.5%         |

Percentage point change

(0.8) pts

1.6 pts

*The 0.8 percentage point decrease in Technical Products Group operating income as a percentage of sales for the third quarter of 2008 from 2007 was primarily the result of:*

inflationary increases related to raw materials such as carbon steel and labor costs; and

*These decreases were partially offset by:*

an increase in sales to electrical markets, which includes selective increases in selling prices to mitigate inflationary cost increases; and

savings realized from the continued success of PIMS initiatives, including lean and supply management activities.

*The 1.6 percentage point increase in Technical Products Group operating income as a percentage of sales for the first nine month of 2008 from 2007 was primarily the result of:*

an increase in sales to electrical markets, which includes selective increases in selling prices to mitigate inflationary cost increases;

savings realized from the continued success of PIMS, including lean and supply management activities;

an increase in sales into electronics markets as orders and sales to our telecommunications customers rebounded and we continued to expand into other vertical markets; and

no longer incurring exit costs recognized in 2007 related to a previously announced 2001 French facility closure.

*These increases were partially offset by:*

inflationary increases related to raw materials such as carbon steel and labor costs.

**Table of Contents****Net interest expense**

|                      | Three months ended      |                         |            |             | Nine months ended       |                         |            |             |
|----------------------|-------------------------|-------------------------|------------|-------------|-------------------------|-------------------------|------------|-------------|
|                      | September<br>27<br>2008 | September<br>27<br>2007 | Difference | %<br>change | September<br>27<br>2008 | September<br>27<br>2007 | Difference | %<br>change |
| <i>In thousands</i>  |                         |                         |            |             |                         |                         |            |             |
| Net interest expense | \$13,735                | \$18,157                | \$(4,422)  | (24.4%)     | \$45,685                | \$51,351                | \$(5,666)  | (11.0%)     |

The 24.4 and 11.0 percentage point decreases in interest expense in the third quarter and first nine months, respectively, of 2008 from 2007 were primarily the result of:

a decrease in outstanding debt; and

favorable impact of lower interest rates.

**Loss on early extinguishment of debt**

On July 8, 2008, we commenced a cash tender offer for all of our outstanding \$250 million aggregate principal 7.85% Senior Notes due 2009 (the Notes). Upon expiration of the tender offer on August 4, 2008, we purchased \$116.1 million aggregate principal amount of the Notes. As a result of this transaction, we recognized a loss of \$4.6 million on early extinguishment of debt. The loss included the write off of \$0.1 million in unamortized deferred financing fees and \$0.6 million in previously unrecognized swap gains, and cash paid of \$5.1 million related to the tender premium and other costs associated with the purchase.

**Provision for income taxes from continuing operations**

|                            | Three months ended      |                         | Nine months ended       |                         |
|----------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|                            | September<br>27<br>2008 | September<br>29<br>2007 | September<br>27<br>2008 | September<br>29<br>2007 |
| <i>In thousands</i>        |                         |                         |                         |                         |
| Income before income taxes | \$64,635                | \$74,148                | \$332,390               | \$234,320               |
| Provision for income taxes | 21,146                  | 14,869                  | 97,522                  | 71,419                  |
| Effective tax rate         | 32.7%                   | 20.1%                   | 29.3%                   | 30.5%                   |

The 12.6 percentage point increase in the effective tax rate in the third quarter of 2008 from 2007 was primarily the result of:

a favorable adjustment that lowered the effective tax rate in the third quarter of 2007 related to the measurement of deferred tax assets and liabilities to account for changes to German tax law enacted on August 17, 2007.

This increase was partially offset by:

higher earnings in lower-tax rate jurisdictions during 2008.

The 1.2 percentage point decrease in the effective tax rate in the first nine months of 2008 from 2007 was primarily the result of:

higher earnings in lower-tax rate jurisdictions during 2008; and

a portion of the gain on the GE Transaction is taxed at a rate of 0%.

These increases were partially offset by:

a favorable adjustment in the third quarter of 2007 related to the measurement of deferred tax assets and liabilities to account for changes to German tax law enacted on August 17, 2007.

We estimate our effective income tax rate for the remaining quarter of 2008 will be between 32% and 33% resulting in a full year effective income tax rate of between 30.0% and 31.0%.

**LIQUIDITY AND CAPITAL RESOURCES**

Cash requirements for working capital, capital expenditures, equity investments, acquisitions, debt repayments, share repurchases and dividend payments have historically been primarily funded from cash generated from operations and availability under existing committed revolving credit facilities as well as in certain instances, public and private debt and equity offerings. We do not anticipate a need for new debt or equity issuances over the foreseeable future.

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We experience seasonal cash flows primarily due to seasonal demand in a number of markets within our Water Group. End-user demand for pool equipment normally follows warm weather trends and is at seasonal highs from April to August. The magnitude of the sales spike is partially mitigated by employing some advance sales early buy programs (generally including extended payment terms and/or additional discounts). Demand for residential and agricultural water systems is also impacted by weather patterns, particularly by heavy flooding and droughts.

The following table presents selected working capital measurements calculated from our monthly operating results based on a 13-month moving average:

|                                      | <b>September<br/>27<br/>2008</b> | <b>December<br/>31<br/>2007</b> | <b>September<br/>29<br/>2007</b> |
|--------------------------------------|----------------------------------|---------------------------------|----------------------------------|
| <i>Days</i>                          |                                  |                                 |                                  |
| Days of sales in accounts receivable | 56                               | 53                              | 54                               |
| Days inventory on hand               | 78                               | 75                              | 76                               |
| Days in accounts payable             | 57                               | 54                              | 54                               |

**Operating activities**

Cash provided by operating activities was \$137.2 million in the first nine months of 2008 compared with cash provided by operating activities of \$229.3 million in the prior year comparable period. The decrease in cash provided by operating activities was primarily due to an increase in cash used for working capital in the first nine months of 2008 and a decrease in Net Income excluding the Gain on sale of interest in subsidiaries versus the same period of last year. In the future, we expect our working capital ratios to improve as we are able to capitalize on our PIMS initiatives.

**Investing activities**

Capital expenditures in the first nine months of 2008 were \$40.1 million compared with \$45.2 million in the prior year period. We currently anticipate capital expenditures for fiscal 2008 will be approximately \$60 million to \$70 million, primarily for capacity expansions in our low cost country manufacturing facilities, new product development, and replacement equipment.

Cash proceeds from the sale of property and equipment of \$4.3 million in 2008 was primarily related to the sale of a facility in our Water Group.

In connection with the GE Transaction, we paid cash of \$1.6 million to acquire additional assets and to fund restructuring initiatives in our Pentair Residential Filtration businesses.

On February 29, 2008, we sold our NPT business to Pool Corporation in a cash transaction for approximately \$30.0 million subject to certain price adjustments. The results of NPT have been reported as discontinued operations for all periods presented. The assets and liabilities of NPT have been reclassified as discontinued operations for all periods presented.

**Financing activities**

Net cash used for financing activities was \$102.5 million in the first nine months of 2008 compared with \$300.2 million provided by financing activities in the prior year period. The reduction primarily relates to the funds borrowed in 2007 for the Porous Media and Jung Pump acquisitions. Financing activities included draw downs and repayments on our revolving credit facilities to fund our operations in the normal course of business, payments of dividends, cash used to repurchase Company stock, cash received from stock option exercises, and tax benefits related to stock-based compensation.

We have a multi-currency Credit Facility. The Credit Facility creates an unsecured, committed revolving credit facility of up to \$800 million, with multi-currency sub facilities to support investments outside the U.S. The Credit Facility expires on June 4, 2012. Borrowings under the Credit Facility will bear interest at the rate of LIBOR plus 0.50%. Interest rates and fees on the Credit Facility vary based on our credit ratings. We believe that internally generated funds and funds available under our Credit Facility will be sufficient to support our normal operations, dividend payments, stock repurchases and debt maturities over the life of the Credit Facility. We have not experienced any disruption in our financing activities currently nor do we anticipate any such disruptions resulting from the

turbulence in the credit markets.

We are authorized to sell short-term commercial paper notes to the extent availability exists under the Credit Facility. We use the Credit Facility as back-up liquidity to support 100% of commercial paper outstanding. As of September 27, 2008, we had \$25.4 million of commercial paper outstanding that matures within 34 days. All of the commercial paper was classified as long-term as we have the intent and the ability to refinance such obligations on a long-term basis under the Credit Facility.

Total availability under our existing Credit Facility was \$506.7 million at September 27, 2008.

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In addition to the Credit Facility, we have \$25.0 million of uncommitted credit facilities, under which we had no borrowings as of September 27, 2008.

On July 8, 2008, we commenced a cash tender offer for all of our outstanding \$250 million aggregate principal of Notes. Upon expiration of the tender offer on August 4, 2008, we purchased \$116.1 million aggregate principal amount of the Notes. As a result of this transaction, we recognized a loss of \$4.6 million on early extinguishment of debt. The loss included the write off of \$0.1 million in unamortized deferred financing fees and \$0.6 million in previously unrecognized swap gains, and cash paid of \$5.1 million related to the tender premium and other costs associated with the purchase.

We were in compliance with all debt covenants as of September 27, 2008.

Our current credit ratings are as follows:

| <b>Rating Agency</b> | <b>Long-Term Debt Rating</b> | <b>Current Rating Outlook</b> |
|----------------------|------------------------------|-------------------------------|
| Standard & Poor's    | BBB                          | Negative                      |
| Moody's              | Baa3                         | Stable                        |

In March 2007, Standard & Poor's Ratings Services revised its current rating outlook on us from stable to negative. At the same time, Standard & Poor's affirmed its long-term debt rating of BBB. Standard & Poor's stated that the outlook revision reflects the additional leverage and stress on credit metrics that will result from the acquisition of Porous Media, which had been announced at the time. The negative outlook indicates the rating could be lowered if financial policies become more aggressive or if operating results are weaker than expected.

As of September 27, 2008, our capital structure consisted of \$1,039.1 million in total indebtedness and \$2,056.0 million in shareholders' equity. The ratio of debt-to-total capital at September 27, 2008 was 33.6 percent, compared with 35.7 percent at December 31, 2007 and 37.8 percent at September 29, 2007. Our targeted debt-to-total capital ratio is approximately 40 percent. We will exceed this target ratio from time to time as needed for operational purposes and/or acquisitions.

Dividends paid in the first nine months of 2008 were \$50.5 million, or \$0.51 per common share, compared with \$45.0 million, or \$0.45 per common share, in the prior year period. We have increased dividends every year for the last 32 years and expect to continue paying dividends on a quarterly basis.

In December 2007, the Board of Directors authorized the repurchase of shares of our common stock during 2008 up to a maximum dollar limit of \$50 million. As of September 27, 2008, we had repurchased an additional 1,094,059 shares for \$38.1 million pursuant to this plan and, accordingly, we have the authority to repurchase additional shares up to a maximum dollar limit of \$11.9 million for the remainder of 2008.

The total gross liability for uncertain tax positions under FASB Interpretation No. 48 at September 27, 2008 is approximately \$25.4 million. We are not able to reasonably estimate the amount by which the estimate will increase or decrease over time; however, at this time, we do not expect a significant payment related to these obligations within the next twelve months.

There have been no material changes with respect to the contractual obligations, other than noted above, or off-balance sheet arrangements described in our 2007 Annual Report on Form 10-K.

**NEW ACCOUNTING STANDARDS**

See Note 2 (New Accounting Standards) of ITEM 1.

**CRITICAL ACCOUNTING POLICIES**

In our 2007 Annual Report on Form 10-K, we identified the critical accounting policies which affect our more significant estimates and assumptions used in preparing our consolidated financial statements. We have not changed these policies from those previously disclosed in our Annual Report.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in our market risk during the quarter ended September 27, 2008. For additional information, refer to Item 7A of our 2007 Annual Report on Form 10-K.

**ITEM 4. CONTROLS AND PROCEDURES****(a) Evaluation of Disclosure Controls and Procedures**

We maintain a system of disclosure controls and procedures designed to provide reasonable assurance as to the reliability of our published financial statements and other disclosures included in this report. Our management evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the quarter ended September 27, 2008 pursuant to Rule 13a-15(b) of the Securities Exchange Act of 1934 (the Exchange Act ). Based upon their evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the quarter ended September 27, 2008 to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms, and to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosures.



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**(b) Changes in Internal Controls**

There was no change in our internal control over financial reporting that occurred during the quarter ended September 27, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of

Pentair, Inc.:

Minneapolis, MN

We have reviewed the accompanying condensed consolidated balance sheets of Pentair, Inc. and subsidiaries (the Corporation ) as of September 27, 2008 and September 29, 2007, and the related condensed consolidated statements of income for the three month and nine month periods ended September 27, 2008 and September 29, 2007, and of cash flows for the nine-month periods ended September 27, 2008 and September 29, 2007. These interim condensed consolidated financial statements are the responsibility of the Corporation s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Pentair, Inc. and subsidiaries as of December 31, 2007, and the related consolidated statements of income, changes in shareholders equity, and cash flows for the year then ended prior to the reclassification for the discontinued operations described in Note 7 to the accompanying condensed consolidated financial statements (not presented herein). Our report dated February 25, 2008, expressed an unqualified opinion on those consolidated financial statements and included an explanatory paragraph relating to the Corporation s changes in its method of accounting for uncertain tax positions in 2007. We also audited the adjustments described in Note 7 that were applied to reclassify the December 31, 2007 consolidated balance sheet of Pentair, Inc. and subsidiaries (not presented herein) for discontinued operations. In our opinion, such adjustments are appropriate and have been properly applied to the previously issued consolidated balance sheet in deriving the accompanying retrospectively adjusted condensed consolidated balance sheet as of December 31, 2007.

*DELOITTE & TOUCHE LLP*

Minneapolis, MN

October 21, 2008

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**PART II OTHER INFORMATION**

**ITEM 1. Legal Proceedings**

*Environmental and Litigation*

There have been no further material developments from the disclosures contained in our 2007 Annual Report on Form 10-K.

*Horizon Litigation*

The Horizon litigation against our subsidiary Esfef Corporation and certain of its subsidiaries by Celebrity Cruise Lines, Inc. ( Celebrity ) was settled by payment of \$35 million to Celebrity in August 2008, a portion of which was covered by insurance. As a result of the settlement, we recorded a charge of \$20.4 million in the second quarter of 2008 which is shown on the line *Legal settlement* in the Condensed Consolidated Statements of Income.

**ITEM 1A. Risk Factors**

There have been no material changes from the risk factors previously disclosed in ITEM 1A. of our 2007 Annual Report on Form 10-K.

**Table of Contents****ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table provides information with respect to purchases we made of our common stock during the third quarter of 2008:

| <b>Period</b>                  | <b>(a)<br/>Total<br/>Number<br/>Shares of<br/>Purchased</b> | <b>(b)<br/>Average<br/>Price<br/>Paid per<br/>Share</b> | <b>(c)<br/>Total Number of<br/>Shares<br/>Purchased as Part<br/>of<br/>Publicly<br/>Announced Plans<br/>or Programs</b> | <b>(d)<br/>Dollar Value of<br/>Shares<br/>that May Yet Be<br/>Purchased Under<br/>the<br/>Plans or<br/>Programs</b> |
|--------------------------------|---|---|---|---|
| June 29 - July 26, 2008        | 138,753   | \$ 33.87  | 138,385   | \$ 22,904,343   |
| July 27 - August 23, 2008      | 168,526   | \$ 36.10  | 139,198   | \$ 17,904,781   |
| August 24 - September 27, 2008 | 182,156   | \$ 37.05  | 162,358   | \$ 11,907,695   |
| <b>Total</b>                   | 489,435   |   | 439,941   |   |

- (a) The purchases in this column include shares repurchased as part of our publicly announced programs and, in addition, 368 shares for the period June 29 - July 26, 2008; 29,328 shares for the period July 27 - August 23, 2008; and 19,798 shares for the period August 24 - September 27, 2008 deemed surrendered to us by participants in our Omnibus Stock Incentive Plan and the Outside Directors Nonqualified Stock Option Plan (the Plans) to satisfy the exercise price or withholding of tax obligations related to the exercise of stock options and non-vested shares.
- (b) The average price paid in this column includes shares repurchased as part of our publicly announced programs and shares deemed surrendered to us by participants in the Plans to satisfy the exercise price or withholding of tax obligations related to the exercise price of stock options and non-vested shares.
- (c) The number of shares in this column represents the number of shares repurchased as part of a publicly announced program to repurchase up to \$50 million of our common stock.
- (d) In December 2007, the Board of Directors authorized the repurchase of shares of our common stock during 2008 up to a maximum dollar limit of \$50 million. As of September 27, 2008, we had purchased 1,094,059 shares for \$38.1 million pursuant to this authorization during 2008. This authorization expires on December 31, 2008.

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**ITEM 6. Exhibits**

**(a) Exhibits**

- 10.1** Amendment to Pentair, Inc. 2008 Omnibus Stock Incentive Plan.
- 15** Letter Regarding Unaudited Interim Financial Information.
- 31.1** Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2** Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1** Certification of Chief Executive Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2** Certification of Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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**SIGNATURE**

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, on October 21, 2008.

PENTAIR, INC.  
Registrant

By /s/ John L. Stauch  
John L. Stauch  
Executive Vice President and Chief Financial  
Officer

By /s/ Mark C. Borin  
Mark C. Borin  
Corporate Controller and Chief Accounting  
Officer  
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**Exhibit Index to Form 10-Q for the Period Ended September 27, 2008**

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