FLOWSERVE CORP
Form 10-K/A
April 27, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K/A

Amendment No. 1

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2002

Commission file number 1-13179

FLOWSERVE CORPORATION

(Exact name of registrant as specified in its charter)

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

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

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
COMMON STOCK, $1.25 PAR VALUE	NEW YORK STOCK EXCHANGE

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: **None**

Indicate by check mark 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 ý No o

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

Indicate by check mark whether the registrant is an accelerated filer. Yes ý No o

The aggregate market value of the common stock held by non-affiliates of the registrant as of June 28, 2002 (the last business day of the registrant s most recently completed second fiscal quarter of 2002) was approximately $1,645,010,809.

The number of shares outstanding of the registrant s common stock as of April 21, 2004 was 54,248,133 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement, dated March 14, 2003, are incorporated by reference into Part III of this Form 10-K/A.

Except where otherwise indicated and unless the context otherwise requires, the terms Flowserve, Company, we, us, our and our Company refer collectively to Flowserve Corporation and its subsidiaries.

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EXPLANATORY NOTE

On February 3, 2004, we announced we would restate our financial results for the nine months ended September 30, 2003 and full years 2002, 2001 and 2000. The restatement predominantly corrects inventory and related balances and cost of sales. For additional discussion regarding the restatement adjustments, see Restatement in Note 2 of the consolidated financial statements and Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations in this annual report on Form 10-K/A for the year ended December 31, 2002 (the Form 10-K/A).

This Form 10-K/A is being filed to amend and restate portions of our Form 10-K for the year ended December 31, 2002 (the Original Form 10-K) as a result of the restatement and comments to the Original Form 10-K received from the Division of Corporate Finance of the Securities and Exchange Commission. Pursuant to Rule 12b-15 promulgated under the Securities Exchange Act of 1934, this Form 10-K/A contains the complete text of the amended and restated items.

Where the items in the Original Form 10-K that are being amended and restated by this Form 10-K/A contained forward-looking information for periods that are now historical, we have updated that information. Other than updating those forward-looking statements and legal proceedings, we have not updated the information contained in this Form 10-K/A for events or transactions occurring after March 12, 2002, the filing date of the Original Form 10-K. Events and transactions have taken place since March 12, 2002 that would have been disclosed in the Original Form 10-K had such events taken place prior to March 12, 2002. As a result, we recommend that you read this Form 10-K/A in conjunction with our reports under the Securities Exchange Act of 1934 filed after March 12, 2002.

This Form 10-K/A includes restatements of the following financial statements:

Consolidated Statements of Operations for the years ended December 31, 2002, 2001 and 2000;

Consolidated Statements of Comprehensive Income / (Loss) for the years ended December 31, 2002, 2001 and 2000;

Consolidated Balance Sheets as of December 31, 2002 and 2001;

Consolidated Statements of Shareholders Equity for the years ended December 31, 2002, 2001 and 2000; and

Consolidated Statements of Cash Flows for the years ended December 31, 2002, 2001 and 2000.

In addition, this Form 10-K/A amends and restates the following items:

Item 1. Business;

Item 3. Legal Proceedings;

Item 6. Selected Financial Data;

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations;

Item 7A. Quantitative and Qualitative Disclosure About Market Risk;

Item 8. Financial Statements and Supplementary Data;

Item 9A. Controls and Procedures; and

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

Except for such matters, no other information is amended and restated by this Form 10-K/A. We have not amended our periodic reports for periods affected by the restatement that ended prior to December 31, 2002. Accordingly, the financial statements, independent auditor s reports and related financial information for the affected periods contained in such reports should no longer be relied upon.

All amounts referenced in this Form 10-K/A for prior periods and prior period comparisons reflect the balances and amounts on a restated basis.

In addition to this Form 10-K/A, we will file amendments to our quarterly reports on Form 10-Q for the quarters ending March 31, June 30 and September 30, 2003.

PART I

ITEM 1. BUSINESS

We believe that we are the world s leading manufacturer and aftermarket service provider of comprehensive flow control systems. Flowserve was incorporated in the State of New York on May 1, 1912. We develop and manufacture precision-engineered flow control equipment for critical service applications where high reliability is required. The flow control system components we produce include pumps, valves and mechanical seals. Our products and services are used in several industries, including, but not limited to, the petroleum, chemical, power generation, water treatment and general industrial industries.

Flowserve conducts its operations through three business segments:

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

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

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

Through each of our segments, we also provide aftermarket replacement parts.

We are not required to carry unusually high amounts of inventory to meet customer delivery requirements nor to assure needed deliveries from suppliers. In fact, we have been working to reduce our overall inventory levels to improve our operational effectiveness and to reduce our working capital needs. We typically do not provide rights of product return to customers, nor do we offer extended payment terms under normal circumstances.

Effective July 1, 2002, we realigned our operating segments. Under the new organization, the Flow Solutions Division includes our seal operations, while our pump service and valve service businesses are included as appropriate in the Flowserve Pump Division and Flow Control Division, respectively. The segment information reported herein reflects the new organizational structure for all periods presented.

For additional information on our business segments, see Note 17 of the consolidated financial statements provided as part of Item 8 of this Form 10-K/A.

FLOWSERVE PUMP DIVISION

Through FPD, we design, manufacture, distribute and service engineered and industrial pumps and pump systems, replacement parts and related equipment principally to industrial markets. FPD s products and services are primarily used by companies that operate in the petroleum, chemical processing, power generating, water treatment and general industrial markets. Our pump systems and components are manufactured at 23 plants in the U.S. and throughout the world. We also manufacture a small portion of our pumps through several foreign joint ventures. We market our pump products, which are primarily sold to end users and engineering and construction companies, through our worldwide sales force, regional service and repair centers, independent distributors and sales representatives.

FPD PRODUCTS

We manufacture more than 100 different pump models ranging from simple fractional horsepower industrial pumps to high horsepower engineered pumps. Our pumps are manufactured in a wide range of metal alloys and with a variety of configurations, including pumps that utilize mechanical seals (sealed pumps) and pumps that do not utilize mechanical seals (Magnetic-Drive pumps).

FPD SERVICES

We provide engineered aftermarket services through our global network of approximately 32 service and quick response centers in 17 countries. Our FPD service personnel provide a comprehensive set of equipment maintenance services for flow management control systems, including repair, advanced diagnostics, installation, commissioning, re-rate and retrofit programs, machining and full service solution offerings. A large portion of our FPD service work is performed on a quick response basis, and we offer 24-hour service in all of our major markets.

The following is a summary list of FPD s general product types and globally recognized brands:

FPD PRODUCT TYPES

Centrifugal Pumps:

- Chemical Process ANSI and ISO
- Petroleum Process API 610
- Horizontal Between Bearing Single-stage
- Horizontal Between Bearing Multi-stage
- Vertical
- Submersible Motor
- Specialty
- Nuclear

Positive Displacement Pumps:

- Reciprocating
- Gear
- Twin Screw

FPD BRAND NAMES

ACEC

Aldrich

Byron Jackson

Cameron

Durco

Duriron

Flowserve

IDP

Pacific

Pleuger

Scienco

Sier-Bath

Worthington-Simpson

United Centrifugal

Western Land Roller

Wilson-Snyder

Worthington

NEW FPD PRODUCT DEVELOPMENTS

Our investments in new product research and development have consistently led to producing more reliable and higher efficiency pumps. The majority of our new FPD products and enhancements are driven by our customers need to achieve higher production rates at lower costs. As a result, we continually work with our customers to develop better pump solutions to improve the availability of their pump systems; however, none of the newly developed FPD products required the investment of a material amount of our assets or was otherwise material.

FPD CUSTOMERS

FPD sells its products to more than 500 customers, including leading engineering and construction firms, original equipment manufacturers (OEM), distributors and end users. FPD s sales mix of original equipment products and aftermarket replacement parts diversifies its business and somewhat mitigates the impact of an economic downturn on its business.

FPD COMPETITION

The pump industry is highly fragmented with more than 50 competitors; however, FPD primarily competes against a relatively limited number of large companies operating on a global scale. Competition is generally based on price, expertise, delivery times, breadth of product offerings, contractual terms, previous installation history and reputation for quality.

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

We believe, based on independent industry sources, that on a global basis we are the third largest industrial pump supplier.

FPD BACKLOG

FPD s backlog of orders at December 31, 2002 was $495.1 million, compared with $551.4 million at December 31, 2001. We shipped approximately 90% of the year end FPD backlog by December 31, 2003.

FLOW SOLUTIONS DIVISION

Through FSD, we design, manufacture and distribute mechanical seals, sealing systems and parts, and provide related services principally to industrial markets. Flow control products require mechanical seals to be replaced throughout the products useful lives. The replacement of mechanical seals is an integral part of aftermarket services. Our mechanical seals are used on a variety of pumps, mixers, compressors, steam turbines and specialty equipment, primarily in the petroleum, chemical processing, power generation and general industrial end-markets. We manufacture mechanical seals at five plants in the U.S. and throughout the world. Through FSD s global network of over 50 service and quick response centers, we provide service, repair and diagnostic services for maintaining components of flow control systems.

FSD s mechanical seal products are primarily marketed through our sales force directly to end users and distributors. A portion of our mechanical seal products is sold directly to OEMs for incorporation into pumps, compressors, mixers or other rotating equipment requiring mechanical seals.

FSD PRODUCTS

FSD designs, manufactures and distributes approximately 180 different models of mechanical seals and sealing systems. We believe our ability to turn around engineered new seal product orders within 24 hours from the customer s request, through design, engineering, manufacturing, testing and delivery, provides us with a leading competitive advantage. Our mechanical seals are critical to the reliable operation of pumps, compressors and mixers for prevention of leakage and emissions of hazardous substances and the reduction of shaft wear caused by non-mechanical seals. We also

manufacture a gas-lubricated mechanical seal that is used in high-speed compressors for gas transmission and in the oil and gas production markets. We continually update our mechanical seals and sealing systems with new technologies.

The following list summarizes FSD s general product types and services and globally recognized brands:

FSD SERVICES

We provide aftermarket services through our network of over 50 service centers and quick response centers located throughout the world. FSD also provides asset management services and condition data point monitoring for rotating equipment. A large portion of our service work (approximately 75%) is performed on a quick response basis, and we offer 24-hour service in all of our major markets.

FSD PRODUCT TYPES

- Cartridge
- Dry-Running
- Metal Bellow
- Elastomeric
- Split
- Gas Barrier
- Service and Repair
- Couplings
- Monitoring and Diagnostics

FSD BRAND NAMES

- BW Seals
- Durametallic

Five Star Seal

Flowserve

Flowstar

GASPAC

Pacific Wietz

Pac-Seal

NEW FSD PRODUCT DEVELOPMENTS

FSD s investments in new product research and development are focused on longer lasting and more efficient products. Approximately 30% of our original equipment mechanical seal sales for 2002 were sales of products developed within the past 5 years. Our latest mechanical seal and seal system innovations include: (1) a sterilizable mixer seal; (2) a high pressure compressor barrier seal; (3) a new web-based asset management tool; (4) an equipment data point monitoring package; (5) as well as numerous product upgrades and improvements. FSD also markets Flowstar.Net, an interactive tool FSD uses to actively monitor and manage information relative to equipment performance, which enhances our customers ability to make informed decisions and respond quickly to plant production problems, extend the life of their production equipment and, therefore, lower maintenance expenses. None of these newly developed FSD products required the investment of a material amount of our assets or was otherwise material.

FSD CUSTOMERS

FSD s mechanical seal products are sold directly to end users and to OEMs for incorporation into pumps, compressors, mixers or other rotating equipment requiring mechanical seals. FSD s mechanical seal sales are diversified among several industries, including petroleum, chemical, power generation, water treatment and general industries.

We have established alliances with over 200 customers. Our customer alliances typically involve a closer working relationship than other customer transactions. Under these alliances, our customers typically agree to place a high percentage of or all of their applicable business with us. In return, we typically commit to a higher level of service,

technical support and prompt product availability than would normally be offered. These alliances provide significant benefits to us, as well as to our customers, by creating a more efficient supply chain through the improvement of equipment reliability, reduction of procurement and inventory costs and increased communication with our customers. Our alliances help us provide products and services to our customers in a timely and cost-effective manner and they are an effective platform for the quick introduction of new products and services, such as condition data point monitoring, to the marketplace.

FSD COMPETITION

FSD competes against a number of manufacturers in the sale of mechanical seals. Our largest global mechanical seal competitor is John Crane, a unit of Smiths Group Plc. We believe, based on independent industry sources, that on a global basis we are the second largest industrial mechanical seals supplier.

FSD BACKLOG

FSD s backlog of orders at December 31, 2002 was $34.4 million, compared with $38.2 million at December 31, 2001. FSD shipped all of its December 31, 2002 backlog during 2003.

FLOW CONTROL DIVISION

Through FCD, we design, manufacture and distribute manual valves, control valves, nuclear valves, actuators and related equipment and provide a variety of flow control-related services. FCD s valve products are an integral part of a flow control system and they are used to control the flow of liquids and gases. Substantially all of FCD s valves are specialized and engineered to perform specific functions within a flow control system.

FCD s products are primarily used by companies that operate in the petroleum, chemical, power generation and general industries. FCD manufactures valves and actuators through 24 major manufacturing plants worldwide. We also manufacture a small portion of our valves through foreign joint ventures. Manual valve products and valve actuators are distributed through our sales force personnel and a network of distributors. Control valves are marketed through sales engineers and service and repair centers or on a commission basis through sales representatives in our principal markets.

In May 2002, we acquired Invensys plc s flow control division (IFC), which is described more fully in the Note 4 of the consolidated financial statements included in this report. The IFC acquisition provided us with an expanded offering of valve types and technologies to better serve our customers flow control needs and broadened our footprint to meet the needs of our increasingly more-global customer base.

FCD PRODUCTS

Our valve, actuator and automated valve accessory offerings represent one of the most comprehensive product portfolios in the flow control industry. Our valves are used in a wide variety of applications from general service to highly corrosive environments, as well as in environments experiencing extreme temperatures and/or pressures and applications requiring zero leakage. FCD sells valves to the chemical, power, petroleum and other industries. In addition to traditional valves, FCD also produces valves that incorporate Smart valve technologies, which integrate high technology sensors, microprocessor controls and digital positioners into a high performance control valve, permitting real time system analysis, system warnings and remote services. We believe we were the first company to introduce Smart valve technologies in response to demands for increased plant automation, more efficient process control and digital communications. FCD offers a growing line of digital products, and it will continue to incorporate digital technologies into its existing products to upgrade performance.

FCD SERVICES

We provide FCD aftermarket services through our network of approximately 50 service and quick response centers located throughout the world. Our service personnel provide a comprehensive set of equipment maintenance services for flow control systems, including repair, advanced diagnostics repair, installation, commissioning, retrofit programs and full machining capabilities. A large portion of our service work is performed on a quick response basis, and we offer 24-hour service in all of our major markets. Services also include leak sealing, line stopping and hot tapping. Offering these types of services provides us access to our customers installed base of flow control products.

The following is a summary list of FCD s general product types and globally recognized brands:

FCD PRODUCT TYPES

Actuator and Accessories

Control Valves

Ball Valves

Lubricated Plug Valves

Pneumatic, Electro Pneumatic and Digital Valves

Digital Communications

Manual Quarter-Turn Valves

Valve Automation Systems

Valve/Actuator Software

Nuclear Valves

Quarter-Turn Actuators

Valve Repair Services

Leak Sealing

Hot Tapping

FCD BRAND NAMES

Accord

Anchor/Darling

Argus

Atomac

Automax

Battig

Durco

Edward

Kammer

Limitorque

McCANNA/MARPAC

NAF

NAVAL

Noble Alloy

Norbro

Nordstrom Audco

PMV

P+W

Serck Audco

Sereg

Schmidt Armaturen

Valtek

Vogt

Worcester Controls

NEW FCD PRODUCT DEVELOPMENTS

Our investments in new FCD product research and development focus on technological leadership and differentiating our product offering. When appropriate, we invest in the redesign of existing products in an effort to improve their performance and continually meet customer needs. None of the newly developed FCD products required the investment of a material amount of our assets or was otherwise material.

FCD CUSTOMERS

FCD s customer mix is diversified within several industries including chemical, petroleum, power and other industries. We sell a mix of original equipment and aftermarket parts to our FCD customers.

FCD COMPETITION

Like the pump market, the valve market is highly fragmented and has undergone a significant amount of consolidation in recent years. Within the valve industry, we believe that the top ten manufacturers, on a global basis, maintain less than 30% of the market. We believe, based on independent industry sources, that on a global basis we are the second largest industrial valve supplier.

FCD BACKLOG

FCD s backlog of orders at December 31, 2002 was $210.8 million, compared with $77.9 million at December 31, 2001. This increase reflects the IFC acquisition. FCD shipped approximately 85% of its December 31, 2002 backlog by December 31, 2003.

GENERAL BUSINESS

COMPETITION

The markets for our products are highly competitive. Competition occurs on the basis of price, technical expertise, delivery, contractual terms, previous installation history and reputation for quality. Delivery speed and the proximity of service centers are important with respect to aftermarket products and services. Customers have traditionally been more likely to rely on us rather than our competitors for aftermarket products relating to our highly engineered and customized products. However, aftermarket competition for standard products is increasing everywhere. Price competition tends to be more significant for OEMs than aftermarket services and has been generally increasing. In the aftermarket portion of our service business, we compete against both large and well-established national or global competitors and, in some markets, against smaller regional and local companies, as well as the in-house maintenance departments of our customers. In the sale of aftermarket products and services, we benefit from the large installed base of pumps and valves which require maintenance, repair and replacement parts.

In the petroleum industry, the competitors for aftermarket services tend to be the customers utilizing their own in-house capabilities. In other industries, except the nuclear power industry, the competitors for aftermarket services tend to be low cost replicators of spare parts and local independent repair shops for our products. We have certain competitive advantages in the nuclear power industry due to our N Stamp, a prerequisite to serve customers in that industry, and due to our considerable base of proprietary knowledge.

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

NEW PRODUCT DEVELOPMENT

We conduct research and development at our own facilities in various locations. Our product development efforts focus on developing new products and on improving versions of existing products. In 2002, 2001 and 2000, we spent

approximately $24.4 million, $23.4 million and $24.8 million, respectively, on Company-sponsored research and development initiatives, primarily developing new products and extending our existing product lines.

Our research and development efforts consist of engineers involved in new product development and improvement of existing products. Additionally, we sponsor consortium programs for research with various universities and conduct limited development work jointly with certain of our vendors, licensees and customers. We believe current expenditures are adequate to sustain our ongoing research and development activities.

CUSTOMERS

We sell to a wide variety of customers in the petroleum, chemical, power generation, water treatment and general industries. No individual customer accounted for more than 10% of our 2002 consolidated revenues.

SELLING AND DISTRIBUTION

Our primary method of distribution is via direct sales by employees assigned to specific regions, industries or products. In addition, we use distributors and sales agents to supplement our direct sales force in countries where business practices or customs make it appropriate, or wherever it is uneconomical to have a direct sales staff. We generate a majority of our sales leads through existing relationships with vendors, customers and prospects or through referrals.

RISKS OF INTERNATIONAL BUSINESS

Sales to foreign destinations, including U.S. export sales, comprised 56% of our sales in 2002, and included business activity in the Middle East. Our activities thus are subject to the customary risks of operating in an international environment, such as military conflicts, unstable political situations, local laws, the potential imposition of trade restrictions or tariff increases and the relationship of the U.S. dollar to other currencies. The impact of these conditions is mitigated somewhat by the strength and diversity of our product lines and geographic coverage. To minimize the impact of foreign exchange rate movements on our operating results, we regularly enter into forward exchange contracts to hedge specific foreign currency denominated transactions, as more fully described in Note 9 of our consolidated financial statements.

For detailed information on revenues to different geographic areas and long-lived assets based on the facilities location, see Note 17 of our consolidated financial statements.

INTELLECTUAL PROPERTY; TRADEMARKS AND PATENTS

We own a number of trademarks and patents relating to the name and design of our products. We consider our trademarks and patents to be an important aspect of our business. In addition, our pool of proprietary information, consisting of know-how and trade secrets relating to the design, manufacture and operation of our products and their use, is considered particularly important and valuable. Accordingly, we attempt to proactively protect such proprietary information. In general, we own the rights to the products which we manufacture and sell and do not depend, in any material way, on any license or franchise to operate. Our trademarks extend indefinitely, while our existing patents will expire 20 years from the dates they were filed, which were at various times in the past. We do not believe that the expiration of any one patent or related patents will adversely or materially impact us.

RAW MATERIALS

The principal raw materials we use in manufacturing our products are readily available and include bar stock and structural steel, castings, fasteners, gaskets, motors, silicon and carbon faces and fluoropolymer components. While substantially all raw materials are purchased from outside sources, we have been able to obtain an adequate supply of raw materials, and do not anticipate any shortages of such materials. We intend to expand worldwide sourcing to capitalize on low cost sources of purchased goods.

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

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

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

EMPLOYEES AND LABOR RELATIONS

We employ approximately 14,000 persons of whom approximately one-half work in the U.S. Our hourly employees at our pump manufacturing plants located in Vernon, California and Phillipsburg, New Jersey, plus those at our valve manufacturing plants in Williamsport, Pennsylvania and Lynchburg, Virginia and at our foundry in Dayton, Ohio, are represented by unions. Additionally, some employees at select facilities in the following countries are unionized or have employee work councils: Argentina, Austria, Belgium, Brazil, Canada, France, Germany, Italy, Mexico, the Netherlands, Spain and the United Kingdom. We believe employee relations throughout our operations are generally satisfactory, including those represented by unions.

ENVIRONMENTAL REGULATIONS AND PROCEEDINGS

We are subject to environmental laws and regulations in all jurisdictions in which we have operating facilities. We periodically make capital expenditures to abate and control pollution and to satisfy environmental requirements. At present, we have no plans for any material capital expenditures for environmental control facilities. However, we have experienced and continue to experience operating costs relating to environmental matters, although certain costs have been offset by successful waste minimization programs. Based on information currently available, we believe that future environmental compliance expenditures will not have a material adverse effect on our financial position. We have established reserves which we believe to be adequate to cover potential environmental liabilities.

EXPORTS

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

Our export sales from the U.S. to foreign unaffiliated customers were $192.4 million in 2002, $167.3 million in 2001 and $148.1 million in 2000.

AVAILABILITY OF FORMS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION

Our shareholders may obtain, without charge, copies of the following documents as filed with the SEC:

- annual reports on Form 10-K,
- quarterly reports on Form 10-Q,
- current reports on Form 8-K,
- changes in beneficial ownership for insiders,
- proxy statements, and
- any amendments thereto,

as soon as reasonably practical after such material is filed with or furnished to the Securities and Exchange Commission. Copies may be obtained by accessing our website at www.flowserve.com or by providing a written request for such copies or additional information regarding our operating or financial performance to Michael E. Conley, Director, Investor Relations, Flowserve Corporation, 5215 N. O Connor Blvd., Suite 2300, Irving, Texas 75039.

We have adopted self-governance guidelines for our Board of Directors. We also have charters for the following committees of the Board: Audit/Finance Committee, Compensation Committee and the Corporate Governance & Nominating Committee. Copies of the Self-Governance Guidelines, as well as the charter for each of the foregoing Board committees, may be obtained as shown above.

ITEM 3. LEGAL PROCEEDINGS

As of December 31, 2002, we were involved as a potentially responsible party (PRP) at two former public waste disposal sites that may be subject to remediation under pending government procedures. The sites are in various stages of evaluation by federal and state environmental authorities. The projected cost of remediating these sites, as well as our alleged fair share allocation, is uncertain and speculative until all studies have been completed and the parties have either negotiated an amicable resolution or the matter has been judicially resolved. At each site, there are many other parties who have similarly been identified, and the identification and location of additional parties is continuing under applicable federal or state law. Many of the other parties identified are financially strong and solvent companies that appear able to pay their share of the remediation costs. Based on our preliminary information about the waste disposal practices at these sites and the environmental regulatory process in general, we believe that it is likely that ultimate remediation liability costs for each site will be apportioned among all liable parties, including site owners and waste transporters, according to the volumes and/or toxicity of the wastes shown to have been disposed of at the sites.

We are a defendant in numerous pending lawsuits (which include, in many cases, multiple claimants) that seek to recover damages for alleged personal injury allegedly resulting from exposure to asbestos-containing products formerly manufactured and/or distributed by us. All such products were used within self-contained process equipment, and we do not believe that there was any emission of ambient asbestos-containing fiber during the use of this equipment.

We are also a defendant in several other product liability lawsuits that are insured, subject to the applicable deductibles, and certain other noninsured lawsuits received in the ordinary course of business. We believe that we have adequately accrued estimated losses for such lawsuits. No insurance recovery has been projected for any of the insured claims, because we currently believe that all will be resolved within applicable deductibles. We are also a party to other noninsured litigation that is incidental to its business, and, in our opinion, will be resolved without a material adverse impact on our financial statements.

In June 2002, we were sued by Ruhrpumpen, Inc. who alleged antitrust violations, conspiracy, fraud and breach of contract claims arising out of our December 2000 sale to Ruhrpumpen of a plant in Tulsa, Oklahoma and a license for eight defined pump lines. The sale agreement had a purchase price of approximately $5.4 million plus other material terms, including Ruhrpumpen s assumption of certain liabilities. Ruhrpumpen subsequently amended its complaint to add Mr. Ronald F. Shuff, our Vice President, Secretary and General Counsel, and two other employees as individual defendants. The sale to Ruhrpumpen was the result of a divestiture agreement we reached with the U.S. Department of Justice (DOJ) in July 2000 in connection with our acquisition of IDP. Our agreement with the DOJ gives it the authority to make inquiries about and otherwise monitor our divestiture. On or about May 13, 2003, we received a letter from the DOJ making inquiry into some of the issues raised by Ruhrpumpen in its lawsuit and seeking information about the divestiture and Ruhrpumpen s lawsuit. The DOJ continues to monitor the lawsuit and the divestiture. During March 2004, the case was tried in the U.S. District Court for the Northern District of Texas. At trial, Ruhrpumpen sought the recovery of over $100 million in actual and exemplary damages. We vigorously contested Ruhrpumpen s allegations and purported damages. At the close of the trial, Ruhrpumpen voluntarily dismissed its claims against Mr. Shuff and the other two employees. We are currently awaiting a ruling from the court as to the remaining claims against the Company.

During the quarter ended September 30, 2003, related lawsuits were filed in federal court, in the Northern District of Texas, alleging that we violated federal securities laws during a period beginning on October 23, 2001 and ending September 27, 2002. The cases were consolidated and a lead plaintiff was appointed by the court. A consolidated amended complaint was filed on February 5, 2004. The consolidated amended complaint, like the earlier individual complaints, also names as individual defendants Mr. C. Scott Greer, Chairman, President and Chief Executive Officer, and Ms. Renée J. Hornbaker, Vice President and Chief Financial Officer, and seeks unspecified compensatory damages and recovery of costs. On March 11, 2004, the court granted the lead plaintiff leave to file a further amended complaint within 15 days of our filing of the finalized restatement of our financial results. We strongly believe that the lawsuit is without merit and plan to vigorously defend the case.

On February 4, 2004, we received an informal inquiry from the SEC requesting the voluntary production of documents and information related to our February 3, 2004 announcement that we would restate our financial results for the nine months ended September 30, 2003 and the full years 2002, 2001 and 2000. In a separate informal inquiry, the SEC requested, and we voluntarily supplied, documents and other information relating to whether our Form 8-K, filed November 21, 2002, adequately fulfilled obligations that may have arisen under Regulation FD. We intend to continue to cooperate with the SEC in these inquiries.

Although none of the aforementioned potential liabilities can be quantified with absolute certainty, we have established reserves covering these possible exposures, which we believe are reasonable based on past experience and available facts. While additional exposures beyond these reserves could exist, none gives rise to any additional liability that can now be reasonably estimated, and we believe any such costs will not have a material adverse impact on our financial position or results of operations. We will continue to evaluate these potential contingent loss exposures and, if necessary, recognize expense as soon as such losses become probable and can be reasonably estimated.

PART II

ITEM 6. SELECTED FINANCIAL DATA

The five-year financial summary set forth in this Item 6 has been restated to reflect the items discussed further in Note 2 to the consolidated financial statements.

(Amounts in thousands, except per share data and ratios)	2002(a) (Restated)	2001(b) (Restated)	2000(c) (Restated)	1999(d)	1998(e)
	Year ending December 31,				
RESULTS OF OPERATIONS					
Sales	**$ 2,251,148**	$ 1,917,332	$ 1,538,293	$ 1,061,272	$ 1,083,086
Gross profit	**677,670**	603,542	504,713	363,344	415,333
Selling, general and administrative expense	**477,433**	411,338	361,619	301,529	291,928
Integration expense	**16,179**	63,043	35,211	14,207	38,326
Restructuring expense	**4,347**	(1,208)	19,364	15,860	
Operating income	**179,711**	130,369	88,519	31,748	85,079
Interest expense	**95,480**	119,636	72,749	15,504	13,175
Earnings before income taxes	**83,652**	13,923	19,764	18,245	73,157
Provision for income taxes	**30,784**	6,560	6,875	6,068	25,502
Earnings before extraordinary items and cumulative effect of change in accounting principle	**52,868**	7,363	12,889	12,177	47,655
Cumulative effect of change in accounting principle					(1,220)
Extraordinary items, net of income taxes	**(7,371)**	(17,851)	(2,067)		
Net earnings (loss)	**45,497**	(10,488)	10,822	12,177	48,875
Average shares outstanding	**52,193**	39,330	37,842	37,856	39,898
Net earnings (loss) per share (diluted)	**$ 0.87**	$ (0.27)	$ 0.29	$ 0.32	$ 1.23
Cash flows from operations	**248,852**	(47,749)	18,431	84,115	54,104
Dividends paid per share				0.56	0.56
Bookings	**2,184,074**	1,975,536	1,521,561	1,039,262	1,082,484
Ending backlog	**733,662**	662,803	659,250	270,647	291,082
PERFORMANCE RATIOS (as a percent of sales)					
Gross profit margin	**30.1%**	31.5%	32.8%	34.2%	38.3%
Selling, general and administrative expense	**21.2%**	21.5%	23.5%	28.4%	26.9%
Operating income	**8.0%**	6.8%	5.8%	3.0%	7.9%
Net earnings (loss)	**2.0%**	(0.5%)	0.7%	1.1%	4.5%
FINANCIAL CONDITION					

Working capital	**$ 503,187**	$ 478,817	$ 469,760	$ 258,128	$ 268,164
Net property, plant and equipment	**463,698**	361,688	405,412	209,976	209,032
Intangibles and other assets	**1,138,865**	783,337	801,128	174,387	173,875
Total assets	**2,617,062**	2,043,928	2,109,119	838,151	870,197
Capital expenditures	**30,875**	35,225	27,819	40,535	38,249
Depreciation and amortization	**65,313**	73,855	57,037	39,599	39,299
Total debt	**1,094,358**	1,040,745	1,129,206	201,135	200,685
Retirement benefits and other liabilities	**328,719**	227,996	260,141	136,207	120,015
Shareholders equity	**721,283**	399,624	305,051	308,274	344,764
FINANCIAL RATIOS					
Return on average shareholders equity	**17.5%**	(17.8)%	19.2%	3.6%	13.1%
Return on average net assets	**5.3%**	5.1%	5.2%	4.9%	13.5%
Net debt to capital ratio	**59.2%**	71.8%	78.1%	35.7%	34.2%
Current ratio	**2.0**	2.1	2.1	2.3	2.2
Interest coverage ratio	**2.4**	1.6	1.9	4.3	9.5

(a) Financial results in 2002 include IFC results from the date of acquisition. Financial results in 2002 include integration expense of $16,179, restructuring expense of $4,347, an extraordinary item of $7,371 net of tax, and a $5,240 purchase accounting adjustment associated with the required write-up and subsequent sale of acquired inventory, resulting in a reduction in after tax net earnings of $24,273.

(b) Financial results in 2001 include integration expense of $63,043, a reduction of Flowserve restructuring expense of $1,208 and an extraordinary item of $17,851 net of tax, resulting in a reduction in after tax net earnings of $57,307.

(c) Financial results in 2000 include Invatec and IDP from the date of the respective acquisitions. Financial results in 2000 include integration expense of $35,211, restructuring expense of $19,364 and an extraordinary item of $2,067 net of tax, resulting in a reduction in after tax net earnings of $37,752.

(d) Financial results in 1999 include integration expense of $14,207 relating to our Flowserver program, restructuring expense of $15,860, other nonrecurring items for inventory and fixed asset impairment of $5,067 (included in costs of sales), and executive separation contracts and certain costs related to fourth-quarter 1999 facility closures of $5,799 (included in selling and administrative expense), resulting in a reduction in net earnings of $27,322.

(e) Financial results in 1998 include integration expense of $38,326, an obligation under an executive employment agreement of $3,803 (included in selling and administrative expense) and, except for operating income, the benefit of the cumulative effect of an accounting change of $1,220, resulting in a reduction in net earnings of $26,062.

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

Management s Discussion and Analysis of Financial Condition and Results of Operations set forth in this Item 7 has been revised to reflect the restatement of our Consolidated Financial Statements for the years ended December 31, 2002, 2001 and 2000 and certain events occurring subsequent to the Original Form 10-K filing, as well as to incorporate certain conforming changes. In addition, disclosures with respect to recently issued accounting standards have been updated.

Restatement

On February 3, 2004, we announced our intention to restate our financial results for the nine months ended September 30, 2003 and the full years and related unaudited quarterly data for 2002, 2001 and 2000 as a result of identifying certain adjustments required to properly state these periods. The accompanying restated consolidated financial statements reflect adjustments made to previously reported financial statements for each of the years ended December 31, 2002, 2001 and 2000. The restatement, primarily affecting our pump and valve segments, principally relates to correcting: inventory amounts and related cost of sales; various non-inventory account balances; the computation of the 2002 and 2001 earnings tax provisions; and the classification of various balance sheet accounts. The restatement reduced reported earnings before income taxes by $8.5 million, $11.7 million and $3.4 million for the years ended December 31, 2002, 2001 and 2000, respectively.

Inventory And Cost Of Sales Adjustments

The inventory and cost of sales adjustments primarily resulted from reconciliation issues at two of our reporting locations due to difficulties associated with converting to new computer systems. The difficulties in executing the conversions and related reconciliation issues resulted in inventory amounts not being properly charged to cost of sales in the appropriate periods. These adjustments reduced reported earnings before income taxes by an aggregate $7.0 million, $10.3 million and $1.2 million for 2002, 2001 and 2000, respectively. Additionally, we restated for adjustments to cost of sales resulting from inventory and related account reconciliations at a limited number of other locations which reduced reported earnings before income taxes by $0.6 million, $0.5 million and $1.0 million for the years ended December 31, 2002, 2001 and 2000.

Other Adjustments

The restatement reduces reported earnings before income taxes by $0.9 million, $0.9 million and $1.2 million for 2002, 2001 and 2000, for adjustments identified during the reconciliation of cash, intercompany transactions, investments in affiliates, equipment and accrued liabilities balances as well as foreign exchange transactions.

Tax Adjustments

The restatement includes the tax effects of the aforementioned adjustments plus adjustments to reduce net earnings by $1.2 million and $1.4 million to correct for certain elements of the computation of the tax provision for 2002 and 2001, respectively.

Balance Sheet Adjustments

We have restated amounts within the balance sheet accounts to appropriately classify tax assets and liabilities, including the establishment of deferred taxes related to the cumulative translation adjustment account.

We also intend to restate our quarterly operating results for each of the first three quarters of 2003 to increase reported earnings before income taxes by $2.1 million to adjust for the aforementioned entries not being recognized in the appropriate periods, including adjustments for certain inappropriate accounting entries made without proper substantiation.

The following tables show the effect of the restatement on our previously issued financial statements:

Increase (decrease) in net earnings (Amounts in millions, except per share data)	**Year ended December 31, 2002**	**2001**	**2000**
Net earnings (loss) - as previously reported	$ 53.0	$ (1.5)	$ 13.2
Adjustments (pretax):			
Inventory and cost of sales adjustments	(7.6)	(10.8)	(2.2)
Other adjustments	(0.9)	(0.9)	(1.2)
Total adjustments (pretax)	(8.5)	(11.7)	(3.4)
Tax adjustments	1.0	2.7	1.0
Net earnings (loss) - as restated	$ 45.5	$ (10.5)	$ 10.8
Net earnings (loss) per share - basic - as previously reported	$ 1.02	$ (0.04)	$ 0.35
Per share effect of restatement adjustments	(0.14)	(0.23)	(0.06)
Net earnings (loss) per share - basic - as restated	$ 0.88	$ (0.27)	$ 0.29
Net earnings (loss) per share - diluted - as previously reported	$ 1.02	$ (0.04)	$ 0.35
Per share effect of restatement adjustments	(0.15)	(0.23)	(0.06)
Net earnings (loss) per share - diluted - as restated	$ 0.87	$ (0.27)	$ 0.29

OVERVIEW

The following discussion and analysis are provided to increase the understanding of, and should be read in conjunction with, the accompanying consolidated financial statements and notes.

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management s discussion and analysis is based on our consolidated financial statements and related footnotes contained within this report. Our more critical accounting policies used in the preparation of the consolidated financial statements are discussed below.

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

The process of preparing financial statements in conformity with accounting principles generally accepted in the U.S. requires the use of estimates and assumptions to determine reported amounts of certain assets, liabilities, revenues and expenses. These estimates and assumptions are based upon the best information available at the time of the estimates or assumptions. The estimates and assumptions could change materially as conditions within and beyond our control change. Accordingly, actual results could differ materially from those estimates. Our most significant estimates include the allowance for doubtful accounts, reserves for excess and obsolete inventories, deferred tax asset valuation allowances, restructuring accruals, legal and environmental accruals, warranty accruals, insurance accruals, pension and postretirement benefit obligations, valuation of goodwill and other long-lived assets, and the expense associated with stock-based compensation. The significant estimates are reviewed quarterly with our Audit/Finance Committee.

Revenue Recognition

Revenues are recognized based on the shipping terms agreed to with the customer and fulfillment of all but inconsequential or perfunctory actions required, which is the point of title transfer, unless the customer order requires formal acceptance under which circumstances revenue is not recognized until formal acceptance has been received. Revenue on service contracts is recognized after the services have been rendered and

accepted by the customer. In addition, our policy requires, prior to shipment, the persuasive evidence of an arrangement, a fixed or determinable sales price and reasonable assurance of collectibility. Revenue for longer-term contracts defined as contracts longer than nine-months in duration, with contract values over $750,000 and progress billings from the customer are recorded on the percentage of completion method calculated on a cost-to-cost basis. Percentage of completion represents approximately 5-10% of consolidated revenues. Revenues generated under fixed fee service and repair contracts, which represent approximately 1% of consolidated revenues, are recognized ratably over the term of the contract, which ranges from 2-5 years.

Allowance For Doubtful Accounts And Credit Risk

Accounts receivable are stated net of the allowance for doubtful accounts.

The allowance for doubtful accounts is established based on estimates of the amount of uncollectible accounts receivable. The amount of the allowance is determined based upon the aging of the receivable, customer credit history, industry and market segment information, economic trends and conditions, credit reports and customer financial condition. Customer credit issues, customer bankruptcies or general economic conditions can affect the estimates.

Credit risk may be mitigated by the large number of customers in our customer base across many different geographic regions and an analysis of the creditworthiness of such customers. Additionally, we maintain a credit insurance policy for our European subsidiaries. Under this policy, we generally receive funds from the third party insurer, net of deductible, in instances where customers covered by the policy are unable to pay.

Inventories

Inventories are stated at the lower-of-cost or market. Cost is determined for U.S. inventories by the last-in, first-out (LIFO) method and for other inventories by the first-in, first-out (FIFO) method. Reserves for excess and obsolete inventories are based on an assessment of slow-moving and obsolete inventories, determined by historical usage and estimated future demand. These estimates are generally not subject to significant volatility, except for product rationalizations generally associated with acquisition integration programs, due to the relatively long life cycle of our products.

Deferred Tax Asset Valuation

We account for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are calculated using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. Valuation allowances reflect the likelihood of the recoverability of any such assets. We record valuation allowances to reflect the estimated amount of deferred tax assets that may not be realized based upon an analysis of existing net operating losses and tax credits by jurisdiction and expectations of our ability to utilize these tax attributes through a review of past, current and estimated future taxable income and establishment of tax strategies. These estimates could be impacted by changes in future taxable income and the results of tax strategies.

Restructuring Reserves

Restructuring reserves are generally established in conjunction with an acquisition. Such reserves reflect many estimates including costs pertaining to employee separation, settlements of contractual obligations and other matters associated with exiting a facility. Restructuring costs related to facilities and employees of an acquired business generally become a component of goodwill, whereas non-acquisition related restructuring costs are recorded as restructuring expense in the statement of operations. Reserve requirements for each restructuring plan are assessed quarterly and susceptible to adjustment due to revisions of cost estimates and other changes in planned restructuring activities.

Legal And Environmental Accruals

The costs relating to legal and environmental liabilities are estimated and recorded when it is probable that a loss has been incurred and such loss is estimable. We have a formal process for assessing the facts and circumstances and recording such contingencies on a case-by-case basis. Assessments of legal and environmental costs are based on information obtained from our independent and in-house experts and our loss experience in similar situations. The estimates may vary in the future due to new developments regarding the facts and circumstances of each

matter.

Warranty Accruals

Warranty obligations are based upon product failure rates, materials usage and service delivery costs. We estimate our warranty provisions based upon an analysis of all identified or expected claims and an estimate of the cost to resolve those claims. The estimates of expected claims are generally a factor of historical claims. Changes in claim rates, differences between actual and expected warranty costs and our facility rationalization activities could impact warranty obligation estimates.

Insurance Accruals

Insurance accruals are recorded based upon an analysis of our claim loss history, insurance deductibles, policy limits and an estimate of incurred but not reported claims. The estimates are based upon information received from our insurance company adjusters. Changes in claims and differences between actual and expected claim losses could impact accruals in the future.

Pension And Postretirement Benefits Obligations

Determination of the value of the pension and postretirement benefits liabilities is based on actuarial valuations. Inherent in these valuations are key assumptions including discount rates, market value of plan assets, expected return on plan assets, life expectancy and assumed rate of increase in wages or in health care costs. Current market conditions, including changes in rates of returns, interest rates and medical inflation rates are considered in selecting these assumptions. Changes in the related pension and postretirement benefit costs may occur in the future due to changes in the assumptions used and changes resulting from fluctuations in the number of plan participants.

Valuation Of Goodwill, Indefinite-Lived Intangible Assets And Other Long-Lived Assets

We test the value of our goodwill and indefinite-lived intangible assets for impairment annually in the fourth quarter and whenever events or circumstances indicate such assets may be impaired. The test involves significant judgment in estimating projections of fair value generated through future performance of each of our reporting units which correlate to our operating segments. The net realizable value of other long-lived assets, including property, plant and equipment, is reviewed periodically, when indicators of potential impairments are present, based upon an assessment of the estimated future cash flows related to those assets.

Due to uncertain market conditions and potential changes in strategy and product portfolio, it is possible that forecasts used to support asset carrying values may change in the future, which could result in non-cash charges that would adversely affect our results of operations and financial condition.

Stock-Based Compensation

We account for our stock option compensation for employees and directors using the intrinsic-value method. All options we grant have an exercise price equal to or in excess of the market price of the underlying stock on the date of grant, therefore, no compensation expense is recognized under the intrinsic-value method of accounting. Awards of restricted stock are valued at the market price of our common stock on the date of grant and recorded as unearned compensation within shareholder s equity. The unearned compensation is amortized to compensation expense over the vesting period of the restricted stock.

See the Accounting Developments section of this Management s Discussion and Analysis for additional information surrounding SFAS No. 148.

RESULTS OF OPERATIONS

In general, 2002 consolidated results and the Flow Control Division results were higher than the corresponding period in 2001 due to our acquisition of Invensys flow control division (IFC) on May 2, 2002. The results for IFC subsequent to the date of acquisition are included in the results for our Flow Control Division. The IFC acquisition is discussed in further detail in the Liquidity and Capital Resources section of this Management s Discussion and Analysis. Pro forma results for 2002 and 2001

referenced throughout this Management s Discussion and Analysis assume that the acquisition of IFC occurred on January 1, 2001 and include estimated purchase accounting and financing impacts.

In general, 2001 consolidated results and the Flowserve Pump Division results were higher than the corresponding period in 2000 due to our acquisition of Ingersoll-Dresser Pump Company (IDP) in August 2000. Pro forma results in 2000 assume the acquisition of IDP took place on January 1, 2000.

All pro forma information is provided solely to enhance understanding of the operating results, not to purport what our results of operations would have been had such transactions or events occurred on the dates specified or to project the our results of operations for any future period.

Sales, Bookings and Backlog

(In millions of dollars)

Sales

We derive our revenues from pumps, valves and seals. Our business is organized around these three distinct types of products into our three business segments: Flowserve Pump Division or FPD (pumps), Flow Control Division or FCD (valves) and Flow Solutions Division or FSD (seals). Within each of the business segments there are sales of various product types: complete units, parts, repairs and other services. Parts or complete units may also be a component of a repair or other service.

Our customers include engineering contractors, original equipment manufacturers (OEMs), end users and distributors. Sales to engineering contractors and OEMs are typically for project orders. Project orders have lead times typically greater than three months. Project orders provide product to our customers either directly or indirectly for their new construction projects or facility enhancement projects. However, some

distributor sales may also be for projects and some OEM sales may not be for projects.

Quick turnaround business, which we also refer to as book and ship business, is defined as orders that are received from the customer and shipped within an approximate three-month period. They are typically for more standard products, parts or services. Each of our three business segments generates quick turnaround business.

Our reporting of trends by product type, customer type and business type are based upon analytical review of individual operational results and our knowledge of their respective businesses as we do not track revenues by these categories.

(In millions of dollars)	**2002 (Restated)**	**2001 (Restated)**	**2000**
Sales	**$ 2,251.1**	$ 1,917.3	$ 1,538.3
Pro forma sales, including IFC	**2,408.5**	2,442.0	n/a(1)

(1) Pro forma information related to IFC for 2000 is not available or required.

Sales increased 17.4% in 2002, compared with a 24.6% increase during 2001. The IFC acquisition and an increased sales volume of mechanical seals positively impacted sales in 2002 by approximately $324 million and $22.7 million, respectively. Sales on a pro forma basis, including IFC, decreased 1.4% during 2002, reflecting the weakness in the quick turnaround business to the chemical, power and general industrial sectors, partially offset by the aforementioned increases. Chemical and industrial pumps, valves and mechanical seals and related services are most dependent on this book and ship business. We believe that the weakness in this business is due to customer deferrals of plant turnarounds and a lower level of capacity utilization due to partial or complete plant closures.

The sales increase in 2000, was largely due to the acquisition of IDP, which added an estimated $ 421.8 million in sales. This was offset partially by lower sales volumes to chemical and general industrial customers due to weakness in the U.S. economy. Unfavorable currency translation of $50.8 million and the divestiture of product lines pursuant to the IDP acquisition and closure or sale of several service operations negatively impacted sales in 2001. Net sales to international customers, including export sales from the U.S., increased to 56% of sales in 2002, compared with 48% in 2001 and 38% in 2000. IFC s proportionately higher mix of international operations contributed to the increase in 2002, while the impact of IDP s international operations contributed to the 2001 increase.

The change in sales is discussed further in the following section on Business Segments.

Bookings And Backlog

(In millions of dollars)	**2002**	**2001**	**2000**
Bookings	**$ 2,184.1**	$ 1,975.5	$ 1,521.6
Pro forma bookings, including IFC	**2,326.2**	2,507.6	n/a(1)
Backlog	**733.7**	662.8	659.3
Pro forma backlog, including IFC	**733.7**	780.1	n/a(1)

(1) Pro forma information related to IFC for 2000 is not available or required.

Bookings, or incoming orders for which there are customer purchase commitments, increased 10.6% in 2002 largely due to the IFC acquisition. Bookings on a pro forma basis decreased in 2002 by 7.2%, which is primarily related to reduced demand for products and services to chemical, power and general industrial customers.

Bookings increased in 2001 largely due to the full year impact of the IDP acquisition. The increase was offset in part by declines in business due to weakness in the U.S. economy, which impacted the chemical and general industrial sectors of the business most significantly in the second half of 2001.

Backlog in 2002 increased 10.7%, largely due to the IFC acquisition. On a pro forma basis, including IFC, backlog decreased 5.9% primarily due to lower bookings in the chemical, power and general industrial sectors despite the booking of several large project orders in 2002.

Business Segments

We manage our operations through three business segments: Flowserve Pump Division (FPD) for engineered pumps, industrial pumps and related services; Flow Solutions Division (FSD) for precision mechanical seals and related services; and Flow Control Division (FCD) for industrial valves, manual valves, control valves, nuclear valves, valve actuators and controls and related services.

Effective July 1, 2002, we realigned our operating segments. The reorganization was undertaken to strengthen end user focus within the segments. Under the new organization, the Flow Solutions Division includes our seal operations, while our pump service and valve service businesses are now managed and thus included in the Flowserve Pump Division and Flow Control Division, respectively. Effective January 1, 2003, we realigned certain small sites between segments. Segment information reflects the new organizational structure for all periods presented.

We believe that special items, while indicative of efforts to integrate IFC and IDP into our business, do not reflect ongoing business results. Earnings before special items are not a recognized measure under generally accepted accounting principles ("GAAP") and should not be viewed as an alternative to GAAP performance measures. Special items included in operating income during each of the three years in the period ended December 31, 2002 are generally associated with the acquisitions of IFC and IDP and include the following:

	Year ended December 31,		
(In millions of dollars)	**2002**	**2001**	**2000**
Integration expense	**$ 16.2**	$ 63.0	$ 35.2
Restructuring expense	**4.3**	(1.2)	19.4
Purchase accounting adjustment for inventory	**5.2**		
Total	**$ 25.7**	$ 61.8	$ 54.6

Sales and operating income before special items for each of the three business segments follows:

	Flowserve Pump Division		
(In millions of dollars)	**2002**	**2001**	**2000**
	(Restated)	**(Restated)**	**(Restated)**
Sales	**$ 1,205.1**	$ 1,170.9	$ 808.6
Pro forma sales, including IDP	**1,205.1**	1,170.9	1,230.4
Operating income (before special items)	**130.1**	134.3	87.5
Integration expense		63.0	35.2
Restructuring expense		(1.2)	19.4
Operating income (after special items)	**130.1**	72.5	32.9
Operating income (before special items) as a percentage of sales	**10.8%**	11.5%	10.8%

Sales of pumps, pump parts and related services for the Flowserve Pump Division (FPD) increased by 2.9% during 2002 and by 44.8% during 2001. The increase in 2002 was largely due to higher sales of engineered pumps for the petroleum and water markets due in part to a backlog that was $56.3 million higher at the beginning of 2002 than the end of 2002. These improvements were partially offset by a lower volume of industrial pumps and service sales to the chemical, power and general industrial markets. The declines in sales to the chemical, power and general industrial sectors were generally due to a lower level of profitability and capacity utilization by the customers. These factors lead to reduced demand as well as some deferred spending by these customers.

The sales increase in 2001 was due to full year inclusion of the IDP acquisition. The 4.8% decrease in pro forma sales during 2001 generally resulted from weakness in the U.S. economy, which impacted quick turnaround sales of industrial pumps to the chemical and general industrial businesses, unfavorable currency effects of an estimated $21.4 million and divestiture of product lines pursuant to the IDP acquisition.

FPD operating income, before special items, decreased 3.1% in 2002, compared with a 53.5% increase in 2001. Operating income in 2002 benefited by $14.0 million from the implementation of SFAS No. 141 and No. 142, but decreased overall due to declines in quick turnaround chemical, power and general industrial businesses, which historically are more profitable than the engineered pump projects. In addition, unfavorable manufacturing burden variances increases of about $3.5 million impacted results primarily due to lower production volumes and

reductions in finished goods inventory in the facilities that manufacture pumps for the chemical, power and general industrial sectors. The reported and pro forma operating income, before special items, increases in 2001 from 2000 primarily resulted from the synergy savings realized from the IDP integration activities, which included the reduction of overlapping sales coverage and the closure and significant downsizing of a number of pump plants.

(In millions of dollars)	Flow Solutions Division 2002	2001	2000
Sales	**$ 350.2**	$ 327.5	$ 327.1
Operating income (before special items)	**64.9**	51.5	46.8
Special items			
Operating income (after special items)	**64.9**	51.5	46.8
Operating income as a percentage of sales	**18.5%**	15.7%	14.3%

Sales of seals for the Flow Solutions Division (FSD) increased by 6.9% in 2002, compared with essentially no increase in 2001. The 2002 increase, despite generally weakened market conditions, reflects the division s emphasis on end user business and its success in establishing customer alliances including longer term fixed fee agreements. Fixed fee alliances are contractual agreements with customers wherein the customer pays us a fixed amount each period (usually monthly) for the term of the agreement. In return for this fixed cost, the customer is entitled to new seals, repairs, upgraded equipment, replacements and maintenance services as defined within the scope of each agreement. We believe that this emphasis combined with a focus on customer responsiveness has contributed to an increase in market share.

Sales for 2001 were relatively flat compared with 2000 as unfavorable currency translation effects primarily associated with the European currencies of an estimated $7.2 million offset the sales volume increase associated with customer alliance agreements.

FSD operating income increased 26.0% in 2002 compared with an increase of 10.0% in 2001. The improvement reflects the benefit of higher sales. Additionally, plant efficiencies resulted from the impact of continuous improvement process projects and bringing in-house of previously outsourced production at generally only variable cost. Operating income in 2002 benefited by $1.2 million from the implementation of SFAS No. 141 and No. 142. Operating income as a percentage of sales increased sequentially over the past three years, reflecting the full year inclusion of continuous improvement process initiatives and the benefit of the restructuring of the North American seal business, which resulted in the closure of a major North American facility and increased capacity in Mexico.

(In millions of dollars)	Flow Control Division 2002 (Restated)	2001 (Restated)	2000
Sales	**$ 725.5**	$ 450.6	$ 440.1
Pro forma sales, including IFC	**882.9**	975.3	n/a(1)
Operating income (before special items)	**44.7**	38.4	39.7
Integration expense	**16.2**		
Restructuring expense	**4.3**		
Purchase accounting adjustment for inventory	**5.2**		
Operating income (after special items)	**19.0**	38.4	39.7
Pro forma operating income (before special items) including IFC	**56.4**	107.7	n/a(1)
Operating income (before special items) as a percentage of sales	**6.2%**	8.5%	9.0%

(1) Pro forma information related to IFC for 2000 is not available or required.

Sales of valves and related products and services for the Flow Control Division (FCD) increased by 61.0% in 2002 primarily due to the acquisition of IFC, compared with a 2.4% increase in 2001. On a pro forma basis for 2002, including IFC, sales decreased 9.5% due to decreased customer demand for valve products and services in the chemical, power and general industrial sectors. Sales in 2001 increased slightly primarily due to increased service opportunities offset by unfavorable currency effects of about $22.2 million and the slowdown in quick turnaround manual valve sales during the second half of 2001.

FCD operating income, before special items, during 2002 increased 16.4%, compared with a 3.3% decrease in 2001. Operating income, before special items, in 2002 benefited by $4.4 million from the implementation of SFAS No. 141 and No. 142. The decline in operating results on a pro forma basis reflects weaker conditions in the chemical, power and general industrial markets, as well as lower production throughput due to lower sales volume combined with a reduction of finished goods inventories, which resulted in unfavorable manufacturing absorption variances. The decline in operating income, before special items, in 2001 reflects a less profitable product mix.

Consolidated Results

Gross profit increased 12.3% to $677.7 million in 2002, compared with $603.5 million in 2001 reflecting the 2002 acquisition of IFC. The gross profit margin was 30.1% for 2002, compared with 31.5% for 2001. On a pro forma basis for 2002 and 2001, including IFC, gross profit was $730.4 million and $778.4 million, which yielded gross profit margins of 30.3% and 31.9%, respectively. Gross profit margin was negatively impacted by an unfavorable product mix of higher sales volumes of lower margin project business and a lower mix of historically more profitable quick turnaround business, including lower volumes of chemical and industrial pumps, industrial valves and service related activities. The quick turnaround business is generally related to more standard products, parts and services. The volumes of this business were down due to reduced profitability of customers in chemical, general industrial, gas pipeline, power and refining industries that are operating either under lower volume conditions or unfavorable price positions due to the economy or currency, unfavorable cost positions due to higher raw material costs or currency, or a combination of the factors above. In addition, gross profit was adversely impacted by an increase of about $42.4 million of unfavorable manufacturing absorption variances, which were attributable to lower production throughput due to lower sales volumes and efforts to reduce finished goods inventories at the facilities that manufacture products for the chemical and general industrial markets. Gross profit and related margin were also impacted in 2002 by a negative $5.2 million purchase accounting adjustment associated with the required write-up and subsequent sale of inventory resulting from the acquisition of IFC. Partially offsetting these negatives was a $1.4 million benefit to gross profit in 2002 from implementing SFAS No. 141 and No. 142 which improved gross profit by $1.4 million for 2002.

Gross profit increased by 19.6% during 2001. The improvement primarily resulted from the full year impact of the IDP acquisition and IDP manufacturing integration synergies that resulted from closing or significantly downsizing a number of pump manufacturing facilities and a number of service and repair facilities. The benefits were partially offset by a less profitable product mix of chemical process pumps, manual valves and service which was caused by a slowdown in the quick turnaround business.

Selling, general and administrative expense was $477.4 million in 2002, $411.3 million in 2001 and $361.6 million in 2000. The increase in 2002 primarily reflects the impact of the IFC acquisition offset in part by the $18.3 million benefit of implementing SFAS No. 141 and No. 142. As a percentage of sales, selling, general and administrative expense was 21.2% compared with 21.5% in 2001 and 23.5% in 2000. The 200 basis-point decrease in the 2001 percentage is generally due to IDP integration savings, resulting from sales force reductions, the IDP headquarters closure and a reduction in incentive compensation due to lower than planned performance and other cost reduction initiatives. Selling, general and administrative expense in 2002 and 2001 on a pro forma basis, including IFC, was $513.3 million and $518.4 million, which represented 21.3% and 21.2% of such amounts as a percentage of pro forma sales.

Restructuring expense of $4.3 million and integration expense of $16.2 million were recognized in 2002 related to the integration of IFC into the Flow Control Division. Restructuring expense represents severance and other exit costs directly related to Flowserve facility closures and reductions in work force. Restructuring expense was a benefit of $1.2 million in 2001 compared with a $19.4 million expense in 2000. The 2001 and 2000 amounts related to the acquisition of IDP, whereas 2002 integration related to IFC. Integration expense represents period costs associated with acquisition-related reorganizations such as relocation of product lines from closed to receiving facilities, realignment of receiving facilities, performance and retention bonuses, idle manufacturing costs, costs related to the integration team and asset impairments. Integration expense of $16.2 million in 2002 relates to the IFC acquisition, whereas the $63.0 million in 2001 and $35.2 million in 2000 related to the integration of IDP into the Flowserve Pump Division. See the section titled Restructuring and Acquisition Related Charges in this Management s Discussion and Analysis for further discussion of restructuring and integration expense.

Operating income of $179.7 million increased 37.8% in 2002 from $130.4 million in 2001. The increase in operating income reflects the IFC acquisition, the benefit of SFAS No. 141 and No. 142 of $19.7 million and reduced integration and restructuring expenses of $41.3 million. These benefits were offset in part by market related factors including a less favorable product mix resulting in lower demand for products and services for chemical, power and general industrial markets. These market factors include a reduced profitability of customers in chemical, general industrial, and power industries that are operating either under lower volume conditions or unfavorable price positions due to the

economy or currency, unfavorable cost positions due to higher raw material costs or currency, or a combination of the factors above. The volumes were lower due to the reduced demand for our products primarily due to the customer market factors discussed above. Additionally, unfavorable absorption variances of

about $42.4 million from the lower volume and reduction in finished goods inventories negatively impacted operating income. On a pro forma basis for 2002 and 2001, including IFC, operating income was $194.8 million and $190.8 million or 8.1% and 7.8%, respectively, as a percentage of pro forma sales. Operating income improved 47.3% in 2001 from 2000 operating income of $88.5 million reflecting the synergy benefits from the IDP acquisition. Operating income in 2001 reflected the full year benefits of the IDP acquisition as well as its related synergy benefits.

Interest expense declined 20.2% to $95.5 million in 2002, compared with $119.6 million in 2001 and $72.7 million in 2000. Approximately $16.3 million of the reduction of interest expense in 2002 resulted from lower debt levels associated with the repayment of one-third of the then outstanding Senior Subordinated Notes in the fourth quarter of 2001 with proceeds from a sale of our common shares. Interest expense was also lower due to lower borrowing spreads associated with the renegotiation of our revolving credit facility and lower interest rates on our variable rate debt. Approximately 65% of our debt was variable rate debt at December 31, 2002. Interest expense declined despite approximately $274 million of incremental borrowings associated with the IFC acquisition due to lower interest rates and $234 million of debt repayments during the year. Increased interest expense in 2001 reflected a full year of interest costs associated with the financing of the IDP acquisition partially offset by the benefit of lower interest rates on our variable rate debt.

Our effective tax rate for 2002 was 36.8%, compared with 47.1% in 2001 and 34.8% in 2000. The 2002 rate was lower than the 2001 rate due to the elimination of goodwill amortization, resulting from the implementation of SFAS No. 141 and No. 142, which was not deductible for income tax purposes. In addition, the relatively low pretax earnings in 2001 compared with 2002 magnified the impact of permanent tax differences, creating a more severe impact to the 2001 effective tax rate. The increase in the rate in 2001 reflects IDP s mix of business conducted in foreign taxing jurisdictions with higher tax rates. The effective tax rate is based upon current earnings and on estimates of future taxable earnings for each domestic and international location as well as the estimated impact of tax planning strategies. Changes in any of these and other factors could impact the tax rate in future periods.

During 2002, we recognized extraordinary expenses of $7.4 million, net of tax, or $0.14 per share compared with $17.9 million or $0.46 per share for 2001. These 2002 expenses relate to the write-off of unamortized prepaid financing fees and other related fees resulting from the debt amendments required pursuant to the IFC acquisition during the second quarter and from the optional debt repayments during the third and fourth quarters of 2002. The 2001 extraordinary item related to the prepayment premium, other direct costs and write-off of unamortized prepaid financing fees and discount as a result of the early extinguishments of $133 million of 12.25% Senior Subordinated Notes, using proceeds from a sale of our common shares. In 2000, we recognized a net of tax extraordinary expense which totaled $2.1 million or $0.05 per share, related to the repayment of our outstanding indebtedness which was required as part of the financing to acquire IDP.

Earnings Per Share - diluted

Net earnings increased in 2002 to $45.5 million, or $0.87 per share, compared with a loss of $10.5 million ($0.27 per share) in 2001 and earnings of $10.8 million ($0.29 per share) in 2000. The implementation of SFAS No. 141 and No. 142 resulted in an increase of $19.7 million or $0.24 per share, to earnings in 2002. Special items in 2002 negatively impacted net earnings by $0.45 per share, including the $0.14 per share extraordinary loss. Special items in 2001 negatively impacted net earnings by $0.83 per

share. Earnings in 2001 benefited from IDP synergies. However, higher interest, integration costs and the aforementioned extraordinary items more than offset those benefits.

Average diluted shares increased by 32.8% to 52.2 million for 2002, compared with 39.3 million in 2001 and 37.8 million in 2000. The 2002 increase in shares reflects the average weighted impact from the equity offering completed in April 2002 to finance the IFC acquisition and the full year impact of the equity offering completed in November 2001, the proceeds of which were used to retire debt. The increase in 2001 reflects the partial year impact from the November 2001 equity offering.

Comprehensive income improved to $25.7 million from losses of $71.0 million in 2001 and $8.5 million in 2000. The 2002 improvement reflects improved net earnings and a favorable foreign currency translation adjustment resulting from the strengthening of the Euro, partially offset by declines in the value of pension plan assets. The decrease in comprehensive income in 2001 resulted from decreased net earnings in part due to IDP integration expenses and an extraordinary loss, increased minimum pension expense and weakening of the Euro and Latin American currencies.

Operating results before special items and pro forma results should not be considered an alternative to operating results calculated in accordance with generally accepted accounting principles.

RESTRUCTURING AND ACQUISITION RELATED CHARGES

Restructuring Costs IFC

In conjunction with the IFC acquisition during 2002, we initiated an integration program designed to reduce costs and eliminate excess capacity by closing seven valve facilities and reducing sales and related support personnel. Our actions, approved and committed to in 2002, are expected to result in a gross reduction of approximately 889 positions and a net reduction of approximately 662 positions based on information available as of the date of this Form 10-K/A filing. Through December 31, 2002, 442 gross positions and 268 net positions had been eliminated pursuant to the program. Net position eliminations represent the gross positions eliminated from the closed facilities offset by positions added at the receiving facilities, which are required to produce the products transferred into the receiving facilities. We expect to realize at least $20 million of annual run rate savings as a result of our integration program. Run rate savings reflect the quantification of synergies achieved at December 31, 2002 on an annualized basis. The savings reflect the benefit of lower payroll and benefit costs resulting from the net position eliminations, partially offset by increased outsourcing costs, and elimination of fixed costs at the closed facilities including depreciation, utilities, lease expense, insurance, taxes and other fixed costs.

Concurrent with the acquisition, we established a restructuring reserve of $11.0 million in the second quarter of 2002, and increased the reserve by $2.8 million and $6.8 million in the third and fourth quarters of 2002 for this program. Costs associated with the closure of our facilities of $4.3 million in 2002 have been recognized as a restructuring expense in the statement of operations. We also recognized a restructuring reserve consisting of $16.3 million of costs and related deferred taxes of $5.1 million. Such costs related to the closure of IFC facilities became part of the purchase price allocation of the transaction. The effect of these closure costs increased the amount of goodwill otherwise recognizable as a result of the IFC acquisition.

The following illustrates activity related to the IFC restructuring reserve:

(Amounts in millions)	Severance	Other Exit Costs	Total
Balance created on June 5, 2002	$ 6.9	$ 4.1	$ 11.0
Additional accruals	6.9	2.7	9.6
Cash expenditures	(3.1)	(1.1)	(4.2)
Balance at December 31, 2002	$ 10.7	$ 5.7	$ 16.4

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Integration Costs - IFC

During 2002, we also incurred acquisition-related integration expense in conjunction with the integration of IFC s operations into Flowserve, which is summarized below:

(Amounts in millions)		2002
Personnel and related costs	$	8.4
Transfer of product lines		3.5
Asset impairments		0.8
Other		3.5
IFC integration expense	$	16.2
Cash expense	$	15.1
Non-cash expense		1.1
IFC integration expense	$	16.2

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

An additional $24.3 million of restructuring and integration costs, including capitalized amounts, were incurred in 2003 for the IFC acquisition. Payments from the restructuring accrual will continue into 2004 and 2005 due to the timing of severance obligations in Europe. The impact of additional restructuring activities will be recorded as obligations are incurred under these programs. To