Woodward, Inc.
Form 10-Q
July 22, 2014
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 June 30, 2014

or

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

For the transition period from _____ to _____

Commission file number 000-08408
WOODWARD, INC.
(Exact name of registrant as specified in its charter)

Delaware	36-1984010
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1000 East Drake Road, Fort Collins, Colorado	80525
(Address of principal executive offices)	(Zip Code)

(970) 482-5811

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

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.

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

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

Yes No

As of July 17, 2014, 65,490,433 shares of the registrant’s common stock with a par value of $0.001455 per share were outstanding.

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PART I – FINANCIAL INFORMATION

Item 1.Financial Statements

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share amounts)

(Unaudited)

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2014	2013	2014	2013
Net sales	$ 524,284	$ 483,759	$ 1,435,793	$ 1,377,611
Costs and expenses:				
Cost of goods sold	372,571	349,482	1,028,065	987,155
Selling, general and administrative expenses	40,468	46,747	113,079	120,371
Research and development costs	34,990	35,487	100,219	99,505
Amortization of intangible assets	8,357	9,769	25,498	27,249
Interest expense	5,972	6,723	18,219	20,196
Interest income	(73)	(68)	(189)	(205)
Other (income) expense, net (Note 16)	(469)	122	(1,266)	(1,030)
Total costs and expenses	461,816	448,262	1,283,625	1,253,241
Earnings before income taxes	62,468	35,497	152,168	124,370
Income tax expense	16,467	11,834	37,986	30,893
Net earnings	$ 46,001	$ 23,663	$ 114,182	$ 93,477
Earnings per share (Note 3):				
Basic earnings per share	$ 0.70	$ 0.35	$ 1.71	$ 1.36
Diluted earnings per share	$ 0.69	$ 0.34	$ 1.68	$ 1.34
Weighted Average Common Shares Outstanding (Note 3):				
Basic	65,845	68,323	66,736	68,506
Diluted	67,147	69,430	68,030	69,698
Cash dividends per share paid to Woodward common stockholders	$ 0.08	$ 0.08	$ 0.24	$ 0.24

See accompanying Notes to Condensed Consolidated Financial Statements.

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS

(In thousands)

(Unaudited)

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2014	2013	2014	2013
Net earnings	$ 46,001	$ 23,663	$ 114,182	$ 93,477
Other comprehensive earnings:				
Foreign currency translation adjustments	(72)	1,056	4,159	(5,002)
Taxes on changes in foreign currency translation adjustments	74	387	368	806
	2	1,443	4,527	(4,196)
Reclassification of net realized losses on derivatives to earnings	24	42	73	128
Unrealized gain on derivatives arising during the period	-	546	-	546
Taxes on changes in derivative transactions	(9)	(223)	(27)	(256)
	15	365	46	418
Minimum retirement benefit liability adjustments (Note 18)				
Net gain (loss) arising during the period	1,193	-	1,193	-
Curtailment arising during the period	(915)	-	(915)	-
Amortization of:				
Net prior service benefit	(22)	(23)	(66)	(69)
Net loss	199	440	588	1,332
Foreign currency exchange rate changes on minimum retirement benefit liabilities	(263)	170	(483)	1,355
Taxes on changes in minimum retirement liability adjustments	31	(214)	(14)	(939)
	223	373	303	1,679
Total comprehensive earnings	$ 46,241	$ 25,844	$ 119,058	$ 91,378

See accompanying Notes to Condensed Consolidated Financial Statements.

WOODWARD, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share amounts)

(Unaudited)

	June 30, 2014	September 30, 2013 (a)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 95,842	$ 48,556
Accounts receivable, less allowance for uncollectible amounts of $7,260 and $8,872, respectively	322,463	381,065
Inventories	469,036	431,744
Income taxes receivable	6,641	14,071
Deferred income tax assets	44,246	43,027
Other current assets	47,971	38,650
Total current assets	986,199	957,113
Property, plant and equipment, net	436,474	350,048
Goodwill	562,691	561,458
Intangible assets, net	263,490	288,775
Deferred income tax assets	17,210	13,926
Other assets	57,009	47,198
Total assets	$ 2,323,073	$ 2,218,518
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	$ -	$ 100,000
Accounts payable	179,420	145,541
Income taxes payable	14,107	7,848
Deferred income tax liabilities	800	800
Accrued liabilities	130,252	161,741
Total current liabilities	324,579	415,930
Long-term debt, less current portion	665,000	450,000
Deferred income tax liabilities	102,909	104,533
Other liabilities	96,588	105,510
Total liabilities	1,189,076	1,075,973
Commitments and contingencies (Note 20)		
Stockholders' equity:		
Preferred stock, par value $0.003 per share, 10,000 shares authorized, no shares issued	-	-
Common stock, par value $0.001455 per share, 150,000 shares authorized, 72,960 shares issued	106	106
Additional paid-in capital	110,237	101,147
Accumulated other comprehensive earnings	19,991	15,115
Deferred compensation	3,878	4,007
Retained earnings	1,292,048	1,193,887
	1,426,260	1,314,262

Treasury stock at cost, 7,477 shares and 4,883 shares, respectively	(288,385)	(167,710)
Treasury stock held for deferred compensation, at cost, 198 shares and 232 shares, respectively	(3,878)	(4,007)
Total stockholders' equity	1,133,997	1,142,545
Total liabilities and stockholders' equity	$ 2,323,073	$ 2,218,518

(a) Retrospectively adjusted as discussed in Note 4, Business acquisitions

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine-Months Ended June 30,	
	2014	2013
Cash flows from operating activities:		
Net earnings	$ 114,182	$ 93,477
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	57,680	56,220
Net (gain) loss on sales of assets	116	(78)
Stock-based compensation	8,739	7,355
Excess tax benefits from stock-based compensation	(2,638)	(4,755)
Deferred income taxes	(5,749)	(36)
Loss on derivatives reclassified from accumulated comprehensive earnings into earnings	73	128
Changes in operating assets and liabilities, net of business acquisitions:		
Accounts receivable	57,151	24,584
Inventories	(38,860)	(20,164)
Accounts payable and accrued liabilities	(6,434)	(16,320)
Current income taxes	16,130	(2,543)
Retirement benefit obligations	(2,676)	(3,290)
Other	(13,824)	(1,561)
Net cash provided by operating activities	183,890	133,017
Cash flows from investing activities:		
Payments for purchase of property, plant, and equipment	(104,530)	(78,515)
Proceeds from sale of assets	258	354
Business acquisitions, net of cash acquired	-	(198,860)
Net cash used in investing activities	(104,272)	(277,021)
Cash flows from financing activities:		
Cash dividends paid	(16,021)	(16,421)
Proceeds from sales of treasury stock	8,380	7,439
Payments for repurchases of common stock	(141,488)	(45,754)
Excess tax benefits from stock compensation	2,638	4,755
Borrowings on revolving lines of credit and short-term borrowings	356,071	97,072
Payments on revolving lines of credit and short-term borrowings	(191,069)	(62,329)
Proceeds from issuance of long-term debt	250,000	200,000
Payments of long-term debt	(300,000)	(41,875)
Payments of debt financing costs	(1,297)	-
Net cash provided by (used in) financing activities	(32,786)	142,887
Effect of exchange rate changes on cash and cash equivalents	454	260
Net change in cash and cash equivalents	47,286	(857)
Cash and cash equivalents at beginning of period	48,556	61,829

Cash and cash equivalents at end of period	$ 95,842	$ 60,972

See accompanying Notes to Condensed Consolidated Financial Statements.

WOODWARD, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands)

(Unaudited)

	Number of shares				Stockholders' equity					
							Accumulated other comprehensive (loss earnings			
	Preferred stock	Common stock	Treasury stock	Treasury stock held for deferred compensation	Common stock	Additional paid-in capital	Foreign currency translation adjustments	Unrealized derivative gains (losses)	Minimum retirement benefit liability adjustments	Total accum other compr (loss) earnin
Balances as of October 1, 2012	-	72,960	(4,536)	(276)	$ 106	$ 97,826	$ 17,447	$ (376)	$ (28,794)	$ (11,
Net earnings	-	-	-	-	-	-	-	-	-	-
Other comprehensive income (loss), net of tax	-	-	-	-	-	-	(4,196)	418	1,679	(2,0
Cash dividends paid	-	-	-	-	-	-	-	-	-	-
Purchases of treasury stock	-	-	(1,395)	-	-	-	-	-	-	-
Sales of treasury stock	-	-	750	-	-	(12,653)	-	-	-	-
Common shares issued from treasury stock for benefit plans	-	-	250	-	-	1,923	-	-	-	-
Tax benefit attributable to exercise of stock options	-	-	-	-	-	4,755	-	-	-	-
Stock-based compensation	-	-	-	-	-	7,355	-	-	-	-
Transfer of stock to deferred	-	-	2	(2)	-	24	-	-	-	-

compensation plan										
Purchases of stock by deferred compensation plan	-	-	-	(2)	-	-	-	-	-	-
Distribution of stock from deferred compensation plan	-	-	-	42	-	-	-	-	-	-
Balances as of June 30, 2013	-	72,960	(4,929)	(238)	$ 106	$ 99,230	$ 13,251	$ 42	$ (27,115)	$ (13,
Balances as of October 1, 2013	-	72,960	(4,883)	(232)	$ 106	$ 101,147	$ 25,742	$ 43	$ (10,670)	$ 15,1
Net earnings	-	-	-	-	-	-	-	-	-	-
Other comprehensive income (loss), net of tax	-	-	-	-	-	-	4,527	46	303	4,87
Cash dividends paid	-	-	-	-	-	-	-	-	-	-
Purchases of treasury stock	-	-	(3,309)	-	-	-	-	-	-	-
Sales of treasury stock	-	-	455	-	-	(4,949)	-	-	-	-
Common shares issued from treasury stock for benefit plans	-	-	260	-	-	2,837	-	-	-	-
Tax benefit attributable to exercise of stock options	-	-	-	-	-	2,463	-	-	-	-
Stock-based compensation	-	-	-	-	-	8,739	-	-	-	-
Purchases of stock by deferred compensation plan	-	-	-	(7)	-	-	-	-	-	-
Distribution of stock from deferred compensation plan	-	-	-	41	-	-	-	-	-	-
	-	72,960	(7,477)	(198)	$ 106	$ 110,237	$ 30,269	$ 89	$ (10,367)	$ 19,9

Balances as of
June 30, 2014
See accompanying Notes to Condensed Consolidated Financial Statements.

WOODWARD, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Note 1. Basis of Presentation

The Condensed Consolidated Financial Statements of Woodward, Inc. ("Woodward" or the "Company") as of June 30, 2014 and for the three and nine-months ended June 30, 2014 and June 30, 2013, included herein, have not been audited by an independent registered public accounting firm. These Condensed Consolidated Financial Statements reflect all normal recurring adjustments that, in the opinion of management, are necessary to present fairly Woodward's financial position as of June 30, 2014, and the statements of earnings, comprehensive earnings, cash flows, and changes in the statement of stockholders' equity for the periods presented herein. The results of operations for the three and nine-months ended June 30, 2014 are not necessarily indicative of the operating results to be expected for other interim periods or for the full fiscal year. Dollar amounts contained in these Condensed Consolidated Financial Statements are in thousands, except per share amounts.

The Condensed Consolidated Balance Sheet as of September 30, 2013 was derived from Woodward's Annual Report on Form 10-K for the fiscal year then ended. During the three-months ended December 31, 2013, Woodward completed purchase accounting valuation estimates related to the acquisition of the Duarte Business (as defined below in Note 4, Business acquisitions) and as a result, retrospectively adjusted the valuations of certain liabilities with a corresponding increase to goodwill and intangible assets as of the acquisition date. The retrospective adjustments amounted to approximately $12,800 and primarily relate to long-term performance obligations and other accrued liabilities. Changes since the acquisition date to the valuations of the assets and liabilities acquired resulted in insignificant changes to Woodward's previously reported earnings and therefore prior reported earnings have not been restated.

The Condensed Consolidated Financial Statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim reporting. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted pursuant to such rules and regulations.

These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in Woodward's most recent Annual Report on Form 10-K filed with the SEC and other financial information filed with the SEC.

Management is required to use estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements, the reported revenues and expenses recognized during the reporting period, and certain financial statement disclosures, in the preparation of the Condensed Consolidated Financial Statements included herein. Significant estimates in these Condensed Consolidated Financial Statements include allowances for losses on receivables, net realizable value of inventories, warranty reserves, cost of sales incentives, useful lives of property and identifiable intangible assets, the evaluation of impairments of property, valuation of identifiable intangible assets and goodwill, income tax and valuation reserves, the valuation of assets and liabilities acquired in business combinations, assumptions used in the determination of the funded status and annual expense of pension and postretirement employee benefit plans, the valuation of stock compensation instruments granted to employees and board members, and contingencies. Actual results could vary materially from Woodward's estimates.

Note 2. Recent accounting pronouncements

From time to time, the Financial Accounting Standards Board ("FASB") or other standards setting bodies issue new accounting pronouncements. Updates to the FASB Accounting Standards Codification ("ASC") are communicated through issuance of an Accounting Standards Update ("ASU").

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers." The purpose of ASU 2014-09 is to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards. The amendments (i) remove inconsistencies and weaknesses in revenue requirements, (ii) provide a more robust framework for addressing revenue issues, (iii) improve comparability of revenue recognition across entities, industries, jurisdictions, and capital markets, (iv) provide more useful information to users of financial statements through improved disclosure requirements, and (v) simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016 (fiscal year 2018 for Woodward), including interim periods within that reporting period. Early adoption is not permitted. An entity should adopt the amendments using one of the following methods: retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying ASU 2014-09 recognized at the date of initial application. Woodward is currently assessing the impact that this guidance may have on its Consolidated Financial Statements.

In February 2013, the FASB issued ASU 2013-02, "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." ASU 2013-02 does not change the current requirements for reporting net income or other comprehensive income in financial statements; however, the amendments require companies to provide information about the amounts reclassified out of accumulated comprehensive income by component. ASU 2013-02 requires a company to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated comprehensive income by respective line items of net income, but only if the amount so reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, a company is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. ASU 2013-02 is effective prospectively for annual reporting periods beginning after December 15, 2012 (fiscal year 2014 for Woodward). The disclosure requirement of ASU 2013-02, which Woodward has adopted, had no material impact on its Consolidated Financial Statements.

Note 3. Earnings per share

Basic earnings per share is computed by dividing net earnings available to common stockholders by the weighted-average number of shares of common stock outstanding for the period.

Diluted earnings per share reflects the weighted-average number of shares outstanding after consideration of the dilutive effect of stock options.

The following is a reconciliation of net earnings to basic earnings per share and diluted earnings per share:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2014	2013	2014	2013
Numerator:				
Net earnings	$ 46,001	$ 23,663	$ 114,182	$ 93,477
Denominator:				
Basic shares outstanding	65,845	68,323	66,736	68,506
Dilutive effect of stock options and restricted stock	1,302	1,107	1,294	1,192
Diluted shares outstanding	67,147	69,430	68,030	69,698
Income per common share:				
Basic earnings per share	$ 0.70	$ 0.35	$ 1.71	$ 1.36
Diluted earnings per share	$ 0.69	$ 0.34	$ 1.68	$ 1.34

The following stock option grants were outstanding during the three and nine-months ended June 30, 2014 and 2013, but were excluded from the computation of diluted earnings per share because their inclusion would have been anti-dilutive:

	Three-Months Ended June 30, 2014	Three-Months Ended June 30, 2013	Nine-Months Ended June 30, 2014	Nine-Months Ended June 30, 2013
Options	677	722	236	239
Weighted-average option price	$ 40.99	$ 34.06	$ 41.05	$ 34.83

The weighted-average shares of common stock outstanding for basic and diluted earnings per share included the weighted-average treasury stock shares held for deferred compensation obligations of the following:

	Three-Months Ended June 30, 2014	Three-Months Ended June 30, 2013	Nine-Months Ended June 30, 2014	Nine-Months Ended June 30, 2013
Weighted-average treasury stock shares held for deferred compensation obligations	206	247	220	262

Note 4. Business acquisitions

Duarte Business Acquisition

On December 27, 2012, Woodward entered into a definitive asset purchase agreement (the "Asset Purchase Agreement") with GE Aviation Systems LLC (the "Seller") and General Electric Company for the acquisition of substantially all of the assets and certain liabilities related to the Seller's thrust reverser actuation systems business located in Duarte, California (the "Duarte Business") for an aggregate purchase price of $200,000. The acquisition was completed on December 28, 2012 and, based on customary purchase price adjustments, Woodward paid cash at closing in the amount of $198,900. Woodward and the Seller have finalized the purchase price adjustment based on the customary post-closing provisions of the Asset Purchase Agreement.

The purchase price of the Duarte Business was as follows:

Cash paid to Seller	$ 198,900
Less cash acquired	(40)
Total purchase price	$ 198,860

The allocation of the purchase price to the assets acquired and liabilities assumed was accounted for under the purchase method of accounting in accordance with ASC Topic 805, "Business Combinations." Assets acquired and liabilities assumed in the transaction were allocated and recorded at their estimated acquisition date fair values using management's best estimate based on available data. Transaction costs associated with the acquisition were expensed as incurred. The Company incurred transaction costs of $304 and $2,011 for the three and nine-months ended June 30, 2013, respectively, which are included in "Selling, general and administrative expenses" in the Condensed Consolidated Statements of Earnings. No additional transaction costs were incurred in the three and nine-months ended June 30, 2014.

During the three-months ended December 31, 2013, Woodward completed its purchase accounting valuation estimates and as a result, retrospectively adjusted the valuations of certain liabilities with a corresponding increase to goodwill and intangible assets as of the acquisition date. The retrospective adjustments amounted to approximately $12,800 and primarily relate to long-term performance obligations and other accrued liabilities. Changes since the acquisition date to the valuations of the assets and liabilities acquired resulted in insignificant changes to Woodward's previously reported earnings and therefore prior reported earnings have not been restated. The allocation of the purchase price to the assets and liabilities assumed was finalized as of December 27, 2013.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition of the Duarte Business:

Accounts receivable	$ 14,245
Inventories	30,149
Other current assets	10,370
Property, plant, and equipment	11,804

Goodwill	98,310
Intangible assets	89,700
Other noncurrent assets	18,097
Total assets acquired	272,675
Other current liabilities	32,509
Other noncurrent liabilities	41,306
Total liabilities assumed	73,815
Net assets acquired	$ 198,860

Goodwill recorded in connection with the acquisition of the Duarte Business, which is deductible for income tax purposes, represents the estimated value of potential expansion with new customers, the opportunity to further develop sales opportunities with new and acquired Duarte Business customers, and other synergies expected to be achieved through the integration of the Duarte Business into Woodward's Aerospace segment.

A summary of the estimated intangible assets acquired, weighted-average useful lives, and amortization methods follows:

	Estimated Amounts	Weighted-Average Useful Life		Amortization Method
Customer relationships and contracts	$ 77,000	20	years	Straight-line
Process technology	5,000	25	years	Straight-line
Backlog	7,700	3	years	Accelerated
Total	$ 89,700			

Assumed liabilities include $4,758 and $17,939 of current and long-term performance obligations, respectively, for contractual commitments that are expected to result in future economic losses.

The Asset Purchase Agreement included commitments for the Duarte Business to continue to provide services to the Seller unrelated to the core business acquired, for which Woodward will continue to be paid by the Seller. Assumed liabilities include $12,985 and $23,215 of current and long-term performance obligations, respectively, for services to be provided to the Seller, offset by $8,103 and $18,097 of current and long-term assets, respectively, related to contractual payments due from the Seller.

Net sales for the Duarte Business subsequent to the date it was acquired by Woodward were $37,929 and $107,062 for the three and nine-months ended June 30, 2014, respectively, and $34,723 and $69,813 for the three and nine-months ended June 30, 2013, respectively. Earnings of the Duarte Business subsequent to the date it was acquired by Woodward for the three and nine-months ended June 30, 2014 cannot be determined on a stand-alone basis due to the integration of the Duarte Business into Woodward's Aerospace segment. Earnings of the Duarte Business subsequent to the date it was acquired by Woodward for the three and nine-months ended June 30, 2013 were slightly accretive to the consolidated net earnings of Woodward. Due to the timing of the acquisition, there were no net sales or operating expenses from the Duarte Business included in the Condensed Consolidated Statements of Earnings for the three-months ended December 31, 2012.

Pro forma results for Woodward giving effect to the acquisition of the Duarte Business

The following unaudited pro forma financial information presents the combined results of operations of Woodward and the Duarte Business as if the acquisition had occurred as of October 1, 2011, the beginning of fiscal year 2012. The pro forma information is presented for information purposes only and is not indicative of the results of operations that would have been achieved if the acquisition and the borrowings used to finance it had taken place at the beginning of fiscal year 2012. The pro forma information combines the historical results of Woodward with the historical results of the Duarte Business for that period.

Prior to the acquisition of the Duarte Business, the Duarte Business was a wholly owned business of the Seller, and as such was not a stand-alone entity for financial reporting purposes. Accordingly, the historical operating results of the Duarte Business may not be indicative of the results that might have been achieved, historically or in the future, if the Duarte Business had been a stand-alone entity. The unaudited pro forma results for the three and nine-months ended June 30, 2014 and June 30, 2013 include amortization charges for acquired intangible assets, eliminations of intercompany transactions, adjustments for depreciation expense for property, plant and equipment, adjustments for acquired performance obligations, transaction costs incurred, adjustments to interest expense, and related tax effects.

The unaudited pro forma results for the three and nine-month periods ended June 30, 2014 and June 30, 2013, compared to the actual results reported in these Condensed Consolidated Financial Statements, were as follows:

	Three-Months Ended June 30, 2014		Three-Months Ended June 30, 2013	
	As reported	Pro forma	As reported	Pro forma
Net sales	$ 524,284	$ 524,284	$ 483,759	$ 483,759
Net earnings	46,001	46,289	23,663	24,639
Earnings per share:				
Basic earnings per share	$ 0.70	$ 0.70	$ 0.35	$ 0.36
Diluted earnings per share	0.69	0.69	0.34	0.35

	Nine-Months Ended June 30, 2014		Nine-Months Ended June 30, 2013	
	As reported	Pro forma	As reported	Pro forma
Net sales	$ 1,435,793	$ 1,435,793	$ 1,377,611	$ 1,408,011
Net earnings	114,182	115,059	93,477	98,609
Earnings per share:				
Basic earnings per share	$ 1.71	$ 1.72	$ 1.36	$ 1.44
Diluted earnings per share	1.68	1.69	1.34	1.41

Note 5. Financial instruments and fair value measurements

Financial assets and liabilities recorded at fair value in the Condensed Consolidated Balance Sheets are categorized based upon a fair value hierarchy established by U.S. GAAP, which prioritizes the inputs used to measure fair value into the following levels:

Level 1: Inputs based on quoted market prices in active markets for identical assets or liabilities at the measurement date.

Level 2: Quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable and can be corroborated by observable market data.

Level 3: Inputs reflect management's best estimates and assumptions of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the valuation of the instruments.

The table below presents information about Woodward's financial assets that are measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques Woodward utilized to determine such fair value. Woodward had no financial liabilities required to be measured at fair value on a recurring basis as of June 30, 2014 or September 30, 2013.

	At June 30, 2014				At September 30, 2013			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Financial assets:								
Cash	$ 76,260	$ -	$ -	$ 76,260	$ 35,839	$ -	$ -	$ 35,839
Investments in money market funds	10,209	-	-	10,209	2,950	-	-	2,950
	9,373	-	-	9,373	9,767	-	-	9,767

Investments in reverse repurchase agreements								
Equity securities	9,803	-	-	9,803	8,285	-	-	8,285
Total financial assets	$ 105,645	$ -	$ -	$ 105,645	$ 56,841	$ -	$ -	$ 56,841

Investments in money market funds: Woodward sometimes invests excess cash in money market funds not insured by the Federal Deposit Insurance Corporation ("FDIC"). Woodward believes that the investments in money market funds are on deposit with creditworthy financial institutions and that the funds are highly liquid. The investments in money market funds are reported at fair value, with realized gains from interest income realized in earnings and are included in "Cash and cash equivalents." The fair values of Woodward's investments in money market funds are based on the quoted market prices for the net asset value of the various money market funds.

Investments in reverse repurchase agreements: Woodward sometimes invests excess cash in reverse repurchase agreements. Under the terms of Woodward's reverse repurchase agreements, Woodward purchases an interest in a pool of securities and is granted a security interest in those securities by the counterparty to the reverse repurchase agreement. At an agreed upon date, generally the next business day, the counterparty repurchases Woodward's interest in the pool of securities at a price equal to what Woodward paid to the counterparty plus a rate of return determined daily per the terms of the reverse repurchase agreement. Woodward believes that the investments in these reverse repurchase agreements are with creditworthy financial institutions and that the funds invested are highly liquid. The investments in reverse repurchase agreements are reported at fair value, with realized gains from interest income realized in earnings, and are included in "Cash and cash equivalents." Since the investments are generally overnight, the carrying value is considered to be equal to the fair value as the amount is deemed to be a cash deposit with no risk of change in value as of the end of each fiscal quarter.

Equity securities: Woodward holds marketable equity securities, through investments in various mutual funds, related to its deferred compensation program. Based on Woodward's intentions regarding these instruments, marketable equity securities are classified as trading securities. The trading securities are reported at fair value, with realized gains and losses recognized in "Other (income) expense, net." The trading securities are included in "Other assets." The fair values of Woodward's trading securities are based on the quoted market prices for the net asset value of the various mutual funds.

Accounts receivable and accounts payable are not remeasured to fair value, as the carrying cost of each approximates its respective fair value. The estimated fair values and carrying costs of other financial instruments that are not required to be remeasured at fair value in the Condensed Consolidated Balance Sheets were as follows:

		At June 30, 2014		At September 30, 2013	
	Fair Value Hierarchy Level	Estimated Fair Value	Carrying Cost	Estimated Fair Value	Carrying Cost
Assets:					
Notes receivable from municipalities	2	15,812	15,103	6,718	8,114
Liabilities:					
Long-term debt, including current portion	2	(711,318)	(665,000)	(588,297)	(550,000)

In fiscal years 2013 and 2014, Woodward received long-term notes from a municipality within the state of Illinois in connection with certain economic incentives related to Woodward's development of a second campus in the greater-Rockford, Illinois area for its Aerospace segment. The fair value of the long-term notes was estimated based on a model that discounted future principal and interest payments received at an interest rate available to the Company at the end of the period for similarly rated municipal notes of similar maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The interest rates used to estimate the fair value of the long-term notes were 3.3% at June 30, 2014 and 4.3% at September 30, 2013.

In fiscal year 2013, Woodward received a long-term note from a municipality within the state of Colorado in connection with certain economic incentives related to Woodward's development of a new campus at its corporate headquarters in Fort Collins, Colorado. The fair value of the long-term note was estimated based on a model that discounted future principal and interest payments received at an interest rate available to the Company at the end of the period for similarly rated municipality notes of similar maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The interest rates used to estimate the fair value of the long-term note were 3.3% at June 30, 2014 and 4.3% at September 30, 2013.

The fair value of long-term debt was estimated based on a model that discounted future principal and interest payments at interest rates available to the Company at the end of the period for similar debt of the same maturity, which is a level 2 input as defined by the U.S. GAAP fair value hierarchy. The weighted-average interest rates used to estimate the fair value of long-term debt were 2.4% and 2.0% as of June 30, 2014 and September 30, 2013, respectively.

Note 6. Derivative instruments and hedging activities

Woodward is exposed to global market risks, including the effect of changes in interest rates, foreign currency exchange rates, changes in certain commodity prices and fluctuations in various producer indices. From time to time, Woodward enters into derivative instruments for risk management purposes only, including derivatives designated as accounting hedges and/or those utilized as economic hedges. Woodward uses interest rate related derivative instruments to manage its exposure to fluctuations of interest rates. Woodward does not enter into or issue derivatives for trading or speculative purposes.

By using derivative and/or hedging instruments to manage its risk exposure, Woodward is subject, from time to time, to credit risk and market risk on those derivative instruments. Credit risk arises from the potential failure of the counterparty to perform under the terms of the derivative and/or hedging instrument. When the fair value of a derivative contract is positive, the counterparty owes Woodward, which creates credit risk for Woodward. Woodward mitigates this credit risk by entering into transactions with only creditworthy counterparties. Market risk arises from the potential adverse effects on the value of derivative and/or hedging instruments that result from a change in interest rates, commodity prices, or foreign currency exchange rates. Woodward minimizes this market risk by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

In June 2013, in connection with Woodward's expected refinancing of current maturities on its existing long-term debt, Woodward entered into a treasury lock agreement with a notional amount of $25,000 that qualified as a cash flow hedge under ASC Topic 815, "Derivatives and Hedging." The objective of this derivative instrument was to hedge the risk of variability in cash flows attributable to changes in the designated benchmark interest rate over a seven-year period related to the future interest payments on a portion of anticipated future debt issuances. An unrealized gain of $546 on the derivative instrument was recorded in "Other current assets" as of June 30, 2013 as the fair value of the cash flow hedge with the offset recorded to reduce accumulated other comprehensive loss ("accumulated OCI").

Woodward did not enter into any derivatives or hedging transactions during the three or nine-months ended June 30, 2014.

The remaining unrecognized gains and losses in Woodward's Condensed Consolidated Balance Sheets associated with derivative instruments that were previously entered into by Woodward, which are classified in accumulated OCI, were net gains of $144 and $71 as of June 30, 2014 and September 30, 2013, respectively.

The following table discloses the impact of derivative instruments in cash flow hedging relationships on Woodward's Condensed Consolidated Statements of Earnings, recognized in interest expense:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2014	2013	2014	2013
Amount of (Income) Expense Recognized in Earnings on Derivative	$ 24	$ 42	$ 73	$ 128
Amount of (Gain) Loss Recognized in Accumulated OCI on Derivative	-	(546)	-	(546)
Amount of (Gain) Loss Reclassified from Accumulated OCI into Earnings	24	42	73	128

Based on the carrying value of the realized but unrecognized gains and losses on terminated derivative instruments designated as cash flow hedges as of June 30, 2014, Woodward expects to reclassify $99 of net unrecognized losses on terminated derivative instruments from accumulated other comprehensive earnings to earnings during the next twelve months.

Note 7. Supplemental statement of cash flows information

	Nine-Months Ended June 30,	
	2014	2013
Interest paid, net of amounts capitalized	$ 26,619	$ 25,463
Income taxes paid	36,345	33,923
Income tax refunds received	1,617	3,371
Non-cash activities:		
Purchases of property, plant and equipment on account	19,193	1,026
Common shares issued from treasury for benefit plans (Note 18)	11,193	9,780
Notes receivable from municipalities for economic development incentives	6,596	2,064
Cashless exercise of stock options	715	2,645
Settlement of receivable through cashless acquisition of treasury shares in connection with the cashless exercise of stock options	871	3,447

Note 8. Accounts receivable

Almost all of Woodward's sales are made on credit and result in accounts receivable, which are recorded at the amount invoiced. In the normal course of business, not all accounts receivable are collected and, therefore, an allowance for losses of accounts receivable is provided equal to the amount that Woodward believes ultimately will not be collected. In establishing the amount of the allowance, customer-specific information is considered related to delinquent accounts, past loss experience, bankruptcy filings, deterioration in the customer's operating results or financial position, and current economic conditions. Accounts receivable losses are deducted from the allowance, and the related accounts receivable balances are written off when the receivables are deemed uncollectible. Recoveries of accounts receivable previously written off are recognized when received.

Consistent with business practice common in China, Woodward's Chinese subsidiary accepts from Chinese customers, in settlement of certain customer accounts receivable, bank drafts issued by creditworthy Chinese banks. Bank drafts are financial instruments issued by Chinese financial institutions as part of financing arrangements between the financial institution and a customer of the financial institution. Bank drafts represent a commitment by the issuing financial institution to pay a certain amount of money at a specified future maturity date to the legal owner of the bank draft as of the maturity date. The maturity date of bank drafts varies, but it is Woodward's policy to only accept bank drafts with maturity dates no more than 180 days from the date of Woodward's receipt of such draft. The issuing financial institution is the obligor, not Woodward's customers. Upon Woodward's acceptance of a bank draft from a customer, such customer has no further obligation to pay Woodward for the related accounts receivable balance. Woodward only accepts bank drafts issued by creditworthy banks as to which the credit risk associated with the bank draft is assessed to be minimal.

The composition of Woodward's accounts receivable at June 30, 2014 and September 30, 2013 follows:

	June 30, 2014	September 30, 2013
Accounts receivable from:		
Customers	$ 279,579	$ 316,983
Other (Chinese financial institutions)	50,144	72,954
Allowance for uncollectible customer amounts	(7,260)	(8,872)
	$ 322,463	$ 381,065

Note 9. Inventories

	June 30,	September 30,

	2014	2013
Raw materials	$ 56,642	$ 67,599
Work in progress	94,204	87,808
Component parts (1)	265,865	229,508
Finished goods	52,325	46,829
	$ 469,036	$ 431,744

(1) Component parts include items that can be sold separately as finished goods or included in the manufacture of other products.

Note 10. Property, plant, and equipment

	June 30, 2014	September 30, 2013
Land and land improvements	$ 57,586	$ 57,562
Buildings and improvements	199,593	195,008
Leasehold improvements	20,926	18,924
Machinery and production equipment	325,916	305,692
Computer equipment and software	104,972	97,538
Office furniture and equipment	24,433	24,400
Other	18,889	14,197
Construction in progress	159,733	81,428
	912,048	794,749
Less accumulated depreciation	(475,574)	(444,701)
Property, plant and equipment, net	$ 436,474	$ 350,048

Woodward is developing a second campus in the greater-Rockford, Illinois area for its Aerospace segment in order to address the growth expected over the next ten years and beyond and to support a substantial number of recently awarded new system platforms, particularly on narrow-body aircraft. Included in construction in progress at June 30, 2014 and September 30, 2013 are $52,410 and $15,691, respectively, of costs associated with the construction of the second campus, including $1,870 and $444, respectively, of capitalized interest.

Woodward is also developing a new campus at its corporate headquarters in Fort Collins, Colorado to support the continued growth of its Energy segment by supplementing its existing Colorado manufacturing facilities and corporate headquarters. Included in construction in progress at June 30, 2014 and September 30, 2013 are $23,401 and $10,514, respectively, of costs associated with the construction of the new campus, including $1,246 and $394, respectively, of capitalized interest.

In addition, in September 2013, Woodward invested in a building site in Niles, Illinois. Woodward is building a new facility on this site for its Aerospace segment and will relocate some of its operations currently residing in nearby Skokie, Illinois to this new facility. Included in construction in progress at June 30, 2014 and September 30, 2013 are $34,130 and $12,067, respectively, of costs associated with the construction of the new facility, including $1,095 and $0 respectively, of capitalized interest.

For the three and nine-months ended June 30, 2014 and June 30, 2013, Woodward recorded depreciation expense of the following:

	Three-Months Ended June 30,		Nine-Months Ended June 30,	
	2014	2013	2014	2013
Depreciation expense	$ 10,489	$ 8,559	$ 32,183	