WOODWARD GOVERNOR CO
Form 10-Q
January 23, 2008

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

Form 10-Q

þ	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the quarterly period ended December 31, 2007**
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934** **For the transition period from to**

Commission file number 0-8408

WOODWARD GOVERNOR COMPANY
(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:

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

Title of each class:	**Name of each exchange on which registered:**
Common stock, par value $.00291 per share	*NASDAQ Global Select Market*

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

As of January 14, 2008, 34,076,647 shares of the common stock with a par value of $0.00291 per share were outstanding.

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PART I FINANCIAL INFORMATION

Item 1. ***Consolidated Financial Statements***

Condensed Consolidated Statements of Earnings

(Unaudited)

	Three Months Ended December 31, 2007	Three Months Ended December 31, 2006
	(In thousands except per share amounts)	
Net sales	$ 272,063	$ 226,248
Costs and expenses:		
Cost of goods sold	190,830	157,744
Selling, general, and administrative expenses	25,980	26,380
Research and developments costs	15,626	13,954
Amortization of intangible assets	1,895	1,726
Interest expense	956	1,192
Interest income	(580)	(623)
Other, net	(1,132)	(777)
Total costs and expenses	233,575	199,596
Earnings before income taxes	38,488	26,652
Income taxes	(13,163)	(8,765)
Net earnings	$ 25,325	$ 17,887
Earnings per share:		
Basic	$ 0.75	$ 0.52
Diluted	$ 0.72	$ 0.51
Weighted-average common shares outstanding:		
Basic	33,942	34,112
Diluted	35,019	35,039
Cash dividends per share	$ 0.11	$ 0.10

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD GOVERNOR COMPANY

Condensed Consolidated Balance Sheets
(Unaudited)

	At December 31, 2007	At September 30, 2007
	(In thousands except per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 61,142	$ 71,635
Accounts receivable, less allowance for losses of $2,281 and $1,886, respectively	140,669	152,826
Inventories, net	191,638	172,500
Income taxes receivable	6,954	9,461
Deferred income tax assets	23,718	23,754
Other current assets	8,601	8,429
Total current assets	432,722	438,605
Property, plant, and equipment, net	159,037	158,998
Goodwill	141,391	141,215
Other intangibles, net	71,331	73,018
Deferred income tax assets	10,194	11,250
Other assets	7,148	6,681
Total assets	$ 821,823	$ 829,767
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Short-term borrowings	$ 5,499	$ 5,496
Current portion of long-term debt	14,957	15,940
Accounts payable	53,601	57,668
Accrued liabilities	61,200	83,890
Total current liabilities	135,257	162,994
Long-term debt, less current portion	34,364	45,150
Deferred income tax liabilities	20,696	19,788
Other liabilities	63,992	57,404
Total liabilities	254,309	285,336
Commitments and contingencies (Note 16)		
SHAREHOLDERS EQUITY:		

Preferred stock, par value $0.003 per share, 10,000 shares authorized, no shares issued				
Common stock, par value $0.00291 per share, 100,000 shares authorized, 36,480 shares issued and outstanding		106		106
Additional paid-in capital		55,379		48,641
Accumulated other comprehensive earnings		26,179		23,010
Deferred compensation		4,743		4,752
Retained earnings		579,033		565,136
		665,440		641,645
Less: Treasury stock at cost, 2,457 shares and 2,616 shares, respectively		(93,183)		(92,462)
Treasury stock held for deferred compensation, at cost, 213 shares and 215 shares, respectively		(4,743)		(4,752)
Total shareholders equity		567,514		544,431
Total liabilities and shareholders equity	$	821,823	$	829,767

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD GOVERNOR COMPANY

Condensed Consolidated Statements of Cash Flow
(Unaudited)

	For the Three Months Ended December 31, 2007	2006
	(In thousands)	
Cash flows from operating activities:		
Net earnings	$ 25,325	$ 17,887
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	9,297	8,249
Postretirement settlement gain		(880)
Contractual pension termination benefit		850
Net gain on sale of property, plant, and equipment	(33)	(10)
Share-based compensation	1,377	1,061
Excess tax benefits from share-based compensation	(5,258)	(1,926)
Deferred income taxes	646	2,061
Reclassification of unrealized losses on derivatives to earnings	52	62
Changes in operating assets and liabilities, net of business acquisition:		
Accounts receivable	13,194	8,660
Inventories	(17,947)	(10,799)
Accounts payable and accrued liabilities	(27,702)	(12,070)
Income taxes receivable	7,589	6,561
Other, net	(167)	(5,952)
Total adjustments	(18,952)	(4,133)
Net cash provided by operating activities	6,373	13,754
Cash flows from investing activities:		
Payments for purchase of property, plant, and equipment	(6,572)	(5,423)
Proceeds from sale of property, plant, and equipment	267	105
Business acquisition, net of cash acquired		(34,564)
Net cash used in investing activities	(6,305)	(39,882)
Cash flows from financing activities:		
Cash dividends paid	(3,726)	(3,415)
Proceeds from sales of treasury stock as a result of exercise of stock options	4,160	559
Purchases of treasury stock	(4,777)	(1,859)
Excess tax benefits from share-based compensation	5,258	1,926
Net payments from borrowings under revolving lines of credit	(31)	(614)
Payments of long-term debt	(11,884)	(11,693)
Net cash used in financing activities	(11,000)	(15,096)

Effect of exchange rate changes on cash and cash equivalents	439	889
Net change in cash and cash equivalents	(10,493)	(40,335)
Cash and cash equivalents at beginning of period	71,635	83,718
Cash and cash equivalents at end of period	$ 61,142	$ 43,383
Supplemental cash flow information:		
Interest expense paid	$ 1,790	$ 2,351
Income taxes paid	2,679	727
Non-cash investing activities:		
Long-term debt assumed in business acquisition		10,319

See accompanying Notes to Condensed Consolidated Financial Statements.

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WOODWARD GOVERNOR COMPANY

Notes to Condensed Consolidated Financial Statements (Unaudited)
(Amounts in thousands, except per share)

(1) Basis of presentation

Woodward Governor Company s (Woodward) Condensed Consolidated Financial Statements for the three months ended December 31, 2007 and 2006, included herein, have not been audited by an independent registered public accounting firm. These Condensed Consolidated Financial Statements reflect all normal recurring adjustments which are, in the opinion of management, necessary to present fairly Woodward s financial position as of December 31, 2007, and the results of operations and cash flows for the periods presented herein. The Condensed Consolidated Balance Sheet as of September 30, 2007 was derived from Woodward s annual report on Form 10-K for the fiscal year ended September 30, 2007. The results of operations for the three months ended December 31, 2007 is not necessarily indicative of the operating results to be expected for other interim periods or for the full year.

The Condensed Consolidated Financial Statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (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 Annual Report on Form 10-K for the fiscal year ended September 30, 2007 and other financial information filed with SEC.

The preparation of the Condensed Consolidated Financial Statements requires management to make use of estimates and assumptions that affect the reported amount of assets and liabilities, revenues and expenses and certain financial statement disclosures. Significant estimates in these Condensed Consolidated Financial Statements include allowances for losses, net realizable value of inventories and related purchase commitments, the cost of sales incentives, useful lives of property and identifiable intangible assets, the evaluation of impairments of property, 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 and the valuation of stock compensation instruments granted to employees, including estimates of the related volatility and expected lives for the instruments. Ultimately realized values could differ from these estimates.

(2) Nature of operations

Woodward operates through three business segments:

Turbine Systems is focused on systems and components that provide energy control and optimization solutions for the aircraft and industrial gas turbine markets.

Engine Systems is focused on systems and components that provide energy control and optimization solutions for the industrial engine and steam turbine markets, which includes power generation, transportation, and process industries.

Electrical Power Systems is focused on systems and components that provide power sensing and energy control systems that improve the security, quality, reliability, and availability of electrical power networks for industrial markets, which includes power generation, power distribution, transportation, and process industries.

(3) Issued but not yet effective accounting standards

SFAS 157: In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal

WOODWARD GOVERNOR COMPANY

Notes to Condensed Consolidated Financial Statements (Continued)

years beginning after November 15, 2007, and interim periods within those fiscal years. As a result, SFAS 157 is effective for Woodward in the first quarter of fiscal 2009. Woodward is currently assessing the impact that SFAS 157 may have on its results of operations and financial position.

SFAS 159: In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115 (SFAS 159). SFAS 159 is expected to expand the use of fair value accounting but does not affect existing standards which require certain assets or liabilities to be carried at fair value. The objective of SFAS 159 is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Under SFAS 159, a company may choose, at specified election dates, to measure eligible items at fair value and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. As a result, SFAS 159 is effective for Woodward in the first quarter of fiscal 2009. Woodward is currently assessing the impact that SFAS 159 may have on its results of operations and financial position.

EITF 07-3: In June 2007, the Emerging Issues Task Force (EITF) issued EITF 07-3, Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities (EITF 07-3). EITF 07-3 addresses the diversity that exists with respect to the accounting for the non-refundable portion of a payment made by a research and development entity for future research and development activities. The EITF concluded that an entity must defer and capitalize non-refundable advance payments made for research and development activities and expense these amounts as the related goods are delivered or the related services are performed. EITF 07-3 is effective for interim or annual reporting periods in fiscal years beginning after December 15, 2007 (fiscal 2009 for Woodward). Woodward is currently evaluating the impact adopting EITF 07-03 may have on its results of operations and financial position.

SFAS 141(R): In December 2007, the FASB issued SFAS No. 141 (Revised) Business Combinations (SFAS 141(R)). SFAS 141(R) is effective for fiscal years beginning after December 13, 2008. As a result, SFAS 141(R) is effective for Woodward in the first quarter of fiscal 2010. SFAS 141(R) establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. SFAS 141(R) also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. Woodward is currently assessing the impact that SFAS 141(R) may have on its results of operations and financial position.

SFAS 160: In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements an Amendment of ARB 51 , (SFAS 160). This statement amends ARB 51 to establish accounting and reporting standards for the noncontrolling interest (minority interest) in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 establishes accounting and reporting standards that require noncontrolling interests to be reported as a component of equity, changes in a parent s ownership interest while the parent retains its controlling interest be accounted for as equity transactions, and any retained noncontrolling equity investment upon the deconsolidation of a subsidiary be initially measured at fair value. SFAS 160 is to be applied prospectively to business combinations consummated on or after the beginning of the first annual reporting period on or after December 15, 2008 (fiscal 2010 for Woodward). Woodward is currently evaluating the impact SFAS 160 may have on its results of operations and financial position.

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Notes to Condensed Consolidated Financial Statements (Continued)

(4) Net earnings per share

Net earnings per share basic is computed by dividing net earnings available to common stockholders by the weighted average number of shares of common stock outstanding for the period. Net earnings per share diluted reflects the potential dilution that could occur if options were exercised.

The average shares outstanding decreased in the first quarter of fiscal 2008 as a result of shares repurchased under Woodward s ongoing share repurchase program. Woodward repurchases common stock at times management deems appropriate, given current market valuations. During the first quarter of fiscal 2008, Woodward completed its accelerated stock repurchase agreement through J.P. Morgan Chase Bank. Woodward purchased a total of 494 common shares in exchange for $31,114 through this program at an average price of $62.95 per common share.

The following is a reconciliation of net earnings to net earnings per share basic and net earnings per share diluted for the first quarters of fiscal 2008 and fiscal 2007:

	Three Months Ended December 31,	
	2007	2006
Numerator:		
Net earnings	$ 25,325	$ 17,887
Denominator:		
Basic	33,942	34,112
Assumed exercise of stock options	1,077	927
Diluted	35,019	35,039
Net earnings per common share:		
Basic	$ 0.75	$ 0.52
Diluted	0.72	0.51

Outstanding stock options totaling 120 and 190 shares for the three months ended December 31, 2007 and 2006, respectively, were not included in the computation of diluted earnings per share because their inclusion would have been anti-dilutive.

(5) Income taxes

Effective Annual Tax Rate for Interim Reporting GAAP requires that the interim period tax provision be determined as follows:

At the end of each quarter, Woodward estimates the tax that will be provided for the fiscal year stated as a percent of estimated ordinary income for the fiscal year. The term ordinary income refers to earnings from continuing operations before income taxes, excluding significant unusual or infrequently occurring items. Discontinued operations are excluded in determining ordinary income.

The estimated annual effective rate is applied to the year-to-date ordinary income at the end of each quarter to compute the year-to-date tax applicable to ordinary income. The tax expense or benefit related to ordinary income in each quarter is the difference between the most recent year-to-date and the prior quarter year-to-date computations.

The tax effects of significant unusual or infrequently occurring items are recognized as discrete items in the interim period in which the events occur. The impact of changes in tax laws or rates on deferred tax amounts, the effects of changes in judgment about beginning of the year valuation allowances and changes in tax

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Notes to Condensed Consolidated Financial Statements (Continued)

reserves resulting from the finalization of tax audits or reviews are examples of significant unusual or infrequently occurring items which are recognized as discrete items in the interim period in which the event occurs.

The determination of the annual effective tax rate is based upon a number of significant estimates and judgments, including the estimated annual pretax income of Woodward in each tax jurisdiction in which it operates and the development of tax planning strategies during the year. In addition, as a global commercial enterprise, Woodward s tax expense can be impacted by changes in tax rates or laws, the finalization of tax audits and reviews, as well as other factors that cannot be predicted with certainty. As such, there can be significant volatility in interim tax provisions.

The following table sets out the tax expense and the effective tax rate for Woodward s continuing operations:

	Three Months Ended December 31,	
	2007	**2006**
Earnings before income taxes	$ 38,488	$ 26,652
Income tax expense	13,163	8,765
Effective tax rate	34.2%	32.9%

Income taxes for the three months ended December 31, 2006, included an expense reduction of $1,177 related to the retroactive extension of the U.S. research and experimentation tax credit. This expense reduction related to the estimated amount of the credit applicable to the period January 1, 2006 through September 30, 2006.

In June 2006, FASB issued FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement 109 (FIN 48), which provides guidance on the financial statement recognition, measurement, reporting and disclosure of uncertain tax positions taken or expected to be taken in a tax return. FIN 48 addresses the determination of whether tax benefits, either permanent or temporary, should be recorded in the financial statements. For those tax benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by the taxing authorities. The amount recognized is measured as the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement.

Woodward adopted the provisions of FIN 48 on October 1, 2007, as required. The change in measurement criteria caused Woodward to recognize a decrease in the retained earnings component of shareholders equity of $7,702.

As of October 1, 2007, the total amount of the gross liability for worldwide unrecognized tax benefits recorded on adoption of FIN 48 and reported in other liabilities in the Condensed Consolidated Balance Sheet was $20,509. Of this amount, $16,316 would impact Woodward s effective tax rate, if recognized. At this time, Woodward estimates that it is reasonably possible that the liability for unrecognized tax benefits will decrease by up to $9,702 in the next twelve months through completion of reviews by various worldwide tax authorities. The change in Woodward s tax liability for unrecognized tax benefits in the first quarter of fiscal 2008 was not significant.

Woodward recognizes interest and penalties related to unrecognized tax benefits in tax expense. As of the date of adoption of FIN 48, Woodward has accrued interest and penalties of $4,396.

Woodward s tax returns are audited by Federal, state, and foreign tax authorities and these audits are at various stages of completion at any given time. Fiscal years remaining open to examination in foreign jurisdictions include 2002 and forward. Woodward is subject to Federal and state income tax examinations for fiscal years 2001 and forward.

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Notes to Condensed Consolidated Financial Statements (Continued)

(6) Inventories

	At December 31, 2007	At September 30, 2007
Raw materials	$ 14,414	$ 10,808
Component parts	108,610	92,737
Work in progress	42,629	36,220
Finished goods	25,985	32,735
	$ 191,638	$ 172,500

(7) Property, plant, and equipment

	At December 31, 2007	At September 30, 2007
Land	$ 12,643	$ 12,469
Buildings and equipment	184,019	182,765
Machinery and equipment	279,837	277,100
Construction in progress	17,444	15,749
	493,943	488,083
Less accumulated depreciation	(334,906)	(329,085)
Property, plant, and equipment, net	$ 159,037	$ 158,998

Depreciation expense totaled $7,402 and $6,523 for the three months ended December 31, 2007 and 2006, respectively.

(8) Goodwill

	September 30, 2007	Additions/ Adjustments	Translation Gains/(Losses)	December 31, 2007
Turbine Systems	$ 86,565	$	$	$ 86,565
Engine Systems	37,736	(675)	(234)	36,827
Electrical Power Systems	16,914	675	410	17,999

Consolidated	$ 141,215	$	$ 176	$ 141,391

(9) Other intangibles net

	At December 31, 2007			At September 30, 2007		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount
Customer relationships:						
Turbine Systems	$ 44,327	$ (14,160)	$ 30,167	$ 44,327	$ (13,791)	$ 30,536
Engine Systems	20,607	(8,472)	12,135	20,607	(8,003)	12,604
Electrical Power Systems	2,679	(554)	2,125	2,609	(424)	2,185
Consolidated	$ 67,613	$ (23,186)	$ 44,427	$ 67,543	$ (22,218)	$ 45,325

WOODWARD GOVERNOR COMPANY

Notes to Condensed Consolidated Financial Statements (Continued)

	At December 31, 2007			September 30, 2007		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount	Gross Carrying Value	Accumulated Amortization	Net Carrying Amount
Other amortizing intangibles:						
Turbine Systems	$ 14,997	$ (6,743)	$ 8,254	$ 14,997	$ (6,567)	$ 8,430
Engine Systems	18,163	(7,290)	10,873	21,828	(8,768)	13,060
Electrical Power Systems	11,255	(3,478)	7,777	11,979	(5,776)	6,203
Consolidated	$ 44,415	$ (17,511)	$ 26,904	$ 48,804	$ (21,111)	$ 27,693

Amortization expense totaled $1,895 and $1,726 for the three months ended December 31, 2007 and 2006, respectively.

Amortization expense associated with current intangibles is expected to be:

Year ending September 30:	
2008 (remaining)	$ 4,473
2009	6,223
2010	6,093
2011	6,050
2012	6,050
Thereafter	42,442
	$ 71,331

(10) Long-term debt

On October 25, 2007, Woodward entered into a Second Amended and Restated Credit Agreement with J.P. Morgan Chase Bank, National Association, Wachovia Bank, N.A., Wells Fargo Bank, N.A. and Deutsche Bank Securities. This agreement increases the initial commitment from $100,000 to $225,000 and also increases the option to expand the commitment from $75,000 to $125,000, for a total of $350,000. The agreement generally bears interest at LIBOR plus 41 basis points to 80 basis points and expires in October 2012. At December 31, 2007 and September 30, 2007, there were no borrowings against the line.

(11) Accrued liabilities

	At December 31, 2007	At September 30, 2007
Salaries and other member benefits	$ 27,760	$ 47,578
Warranties	5,414	5,675
Taxes, other than income	4,707	6,682
Accrued retirement benefits	6,079	6,132
Deferred compensation	14	3,685
Other, net	17,226	14,138
	$ 61,200	$ 83,890

Provisions of the sales agreements include product warranties customary to such agreements. Accruals are established for specifically identified warranty issues that are probable to result in future costs. Warranty costs are

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Notes to Condensed Consolidated Financial Statements (Continued)

accrued on a non-specific basis whenever past experience indicates a normal and predictable pattern exists. Changes in accrued product warranties were as follows:

	2007
Balance, September 30,	$ 5,675
Accruals related to warranties issued during the period	967
Accruals related to pre-existing warranties	991
Settlements of amounts accrued	(2,257)
Foreign currency exchange rate changes	38
Balance, December 31,	$ 5,414

(12) Other liabilities

	At December 31, 2007	At September 30, 2007
Net accrued retirement benefits, less amounts recognized with accrued liabilities	$ 45,189	$ 46,145
Other, net	18,803	11,259
	$ 63,992	$ 57,404

(13) Retirement benefits

The components of the net periodic pension cost related to continuing operations are as follows:

	Three Months Ended December 31, 2007	2006
Retirement pension benefits United States:		
Service cost	$	$
Interest cost	281	259
Expected return on plan assets	(341)	(329)
Amortization of:		
Net actuarial loss	30	61
Prior service cost	(65)	(65)

Net periodic benefit	$	(95)	$	(74)
Contributions	$		$	

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Notes to Condensed Consolidated Financial Statements (Continued)

	Three Months Ended December 31, 2007	Three Months Ended December 31, 2006
Retirement pension benefits other countries:		
Service cost	$ 237	$ 320
Interest cost	726	628
Expected return on plan assets	(761)	(589)
Amortization of:		
Transition obligation	23	23
Net actuarial loss	47	93
Prior service cost	(2)	(2)
Contractual termination benefits		850
Net periodic cost	$ 270	$ 1,323
Contributions	$ 1,028	$ 584

The components of the net periodic retirement healthcare benefits related to continuing operations are as follows:

Retirement healthcare benefits:		
Service cost	$ 61	$ 74
Interest cost	613	619
Amortization of:		
Net actuarial loss	48	65
Prior service cost	(630)	(630)
Settlement gains		(880)
Net periodic (benefit) cost	$ 92	$ (752)
Contributions	$ 549	$ 459

Woodward expects its contributions for retirement pension benefits will be $0 in the United States and $2,913 in other countries in 2008. Woodward also expects its contributions for retirement healthcare benefits will be $3,276 in 2008, less amounts received as federal subsidies. The exact amount of cash contributions made to these plans in any year is dependent upon a number of factors including minimum funding requirements in the jurisdictions in which Woodward operates and arrangements made with trustees of certain foreign plans. As a result, the actual funding in fiscal 2008 may differ from the current estimate.

Woodward is entitled to a federal subsidy under the Medicare Prescription Drug, Improvement and Modernization Act of 2003. Woodward received no subsidy for the three months ended December 31, 2007 ($433 for the three months ended December 31, 2006). Woodward currently expects to receive an additional $542 during the year ending September 30, 2008. Woodward paid prescription drug benefits of $813 and $678 during the three months ended December 31, 2007 and 2006, respectively. Woodward expects to pay additional prescription drug benefits of approximately $1,800 for the year ending September 30, 2008.

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Notes to Condensed Consolidated Financial Statements (Continued)

(14) Accumulated and other comprehensive earnings

Accumulated other comprehensive earnings, which totaled $26,179 at December 31, 2007, consisted of the following items:

Accumulated foreign currency translation adjustments:	
Beginning balance	$ 27,614
Translation adjustments	3,531
Ending balance	$ 31,145
Accumulated unrealized derivative losses:	
Beginning balance	$ (331)
Reclassification to interest expense	52
Taxes associated with interest reclassification	(20)
Ending balance	$ (299)
Accumulated minimum pension liability adjustments:	
Beginning balance	$ (4,273)
Minimum pension liability adjustment	(469)
Taxes associated with minimum pension liability	75
Ending balance	$ (4,667)

(15) Total comprehensive earnings

	Three Months Ended December 31, 2007	2006
Net earnings	$ 25,325	$ 17,887
Other comprehensive earnings:		
Foreign currency translation adjustments	(3,531)	2,985
Reclassification of unrealized losses on derivatives to earnings	(32)	38
Minimum pension liability adjustment	394	98
Total comprehensive earnings	$ 22,156	$ 21,008

(16) Contingencies