FLOW INTERNATIONAL CORP
Form 424B3
April 26, 2007
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Filed Pursuant to Rule 424(b)(3)
Registration No. 333-125113

7,183,018 Shares

Common Stock

This prospectus relates to the offer and sale of up to 6,779,718 outstanding shares of the common stock of Flow International Corporation, a Washington corporation, and up to 403,300 shares that may be issued on the exercise of outstanding warrants. Such shares may be offered and sold from time to time by the persons described in this prospectus under the heading Selling Shareholders or by pledgees, donees, transferees, assignees or other successors-in-interest of such persons (collectively, the Selling Shareholders). In the original Registration Statement, we registered up to 17,799,179 outstanding shares of common stock of Flow International Corporation and up to 2,188,091 shares that may be issued on the exercise of outstanding warrants. Certain of the original Selling Shareholders have sold all of their shares, others have sold some of their shares, and still others continue to hold the original amount of shares. As used in this prospectus, we, us, our and similar expressions refer to Flow International Corporation and its subsidiaries.

The Selling Shareholders may offer their shares from time to time through or to one or more underwriters, brokers or dealers, on the NASDAQ Stock National Market at market prices prevailing at the time of sale, in one or more negotiated transactions at prices acceptable to the Selling Shareholders or in private transactions. We will not receive any proceeds from the sale of shares by the Selling Shareholders. In connection with any sales, the Selling Shareholders and any underwriters, agents, brokers or dealers participating in such sales may be deemed to be underwriters within the meaning of the Securities Act.

We will pay the expenses related to the registration of the shares covered by this prospectus. The Selling Shareholders will pay commissions and selling expenses, if any, incurred by them.

Our common stock trades on the NASDAQ National Market under the symbol FLOW. On April 24, 2007, the closing price of one share of our common stock was $11.35.

Investing in our securities involves risks. See Risk Factors beginning on page 7 of this prospectus.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this prospectus is April 25, 2007.

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You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with different information. An offer to sell these securities is not being made in any state where the offer is not permitted. You should not assume that the information contained in this prospectus or any prospectus supplement is accurate as of any date other than the date of such documents. Our business, financial condition, results of operations and prospects may have changed since that date.

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ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission using the SEC s shelf registration rules. Under the shelf registration rules, using this prospectus and, if required, one or more prospectus supplements, the Selling Shareholders may sell from time to time, in one or more offerings, the shares of common stock covered by this prospectus. The shares covered by this prospectus include 6,579,718 outstanding shares of common stock and 403,300 shares of common stock issuable upon the exercise of warrants.

This prospectus also covers any shares of common stock that may become issuable pursuant to anti-dilution adjustment provisions that would increase the number of shares issuable upon exercise of the warrants as a result of stock splits, stock dividends or similar transactions.

A prospectus supplement may add, update or change information contained in this prospectus. We recommend that you read carefully this entire prospectus, especially the section entitled Risk Factors beginning on page 13, together with any supplements before making a decision to invest in our common stock.

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PROSPECTUS SUMMARY

This summary highlights key aspects of the information contained elsewhere in this prospectus. This summary does not contain all the information you should consider before investing in our common stock. You should read this entire prospectus carefully, especially the risks of investing in our common stock discussed under Risk Factors beginning on page 7, current events beginning on page 17 and our consolidated financial statements and the notes to those consolidated financial statements beginning on page F-1, before making an investment decision.

THE COMPANY

We design, develop, manufacture, market, install and service ultrahigh-pressure, or UHP, water pumps and UHP water management systems. Our core competency is the design and manufacture of UHP water pumps. Our UHP water pumps pressurize water from 40,000 to over 100,000 pounds per square inch (psi) and are integrated with water delivery systems so that water can be used to cut or clean material or pressurize food. Our products include standard and specialized waterjet cutting and cleaning systems. In addition to UHP water pumps and related systems, we provide non-UHP automation and articulation systems, primarily to the automotive industry.

Our UHP technology has three broad applications: cutting, cleaning and food processing. In cutting and cleaning applications, the ultrahigh-pressure created by our pumps is released through a small orifice to create a jet of water. In food processing, we supply UHP pumps to Avure Technologies, Inc., a company we sold in 2005, which uses pressure to kill spoilage bacteria and pathogens in food products placed inside a pressure vessel.

The primary application of our UHP water pumps is cutting. In cutting applications, pressures from 50,000 to 87,000 psi create a thin stream of water traveling at three or more times the speed of sound which can cut both metallic and nonmetallic materials. UHP water pumps are used in aerospace, automotive, disposable products, food, glass, job shop, sign, metal cutting, marble, tile and other stone cutting, and paper slitting and trimming applications. Waterjet cutting is recognized as a more flexible alternative to traditional cutting methods such as lasers, saws or plasma. It is often faster, has greater versatility in the types of materials it can cut and eliminates the need for secondary processing operations. We also manufacture a waterjet product line used in cleaning, where pressures in the range of 40,000 to 55,000 psi are used in industrial cleaning, surface preparation, construction, and petro-chemical and oil field applications.

On October 31, 2005, consistent with our strategy to divest operations that are not part of our core UHP water pump business, we sold our General Press operations and the non-UHP portion of our Food reportable segment (the Avure Disposition). Included in the Avure Disposition were our Avure Technologies, Incorporated, Flow International FPS AB, Avure Technologies AB subsidiaries, and our 51% interest in Flow Autoclave Systems (together, the Avure Business). The Avure Business became a discontinued operation in accordance with FAS 144 *Accounting for the Impairment or Disposal of Long-Lived Assets* at the time it was sold and has been represented that way in the Consolidated Statements of Operations in the financial statements. In connection with the sale we agreed to continue to supply UHP pumps to the Avure Business.

Our principal executive offices are at 23500 64th Avenue South, Kent, WA 98032 and our telephone number is (253) 850-3500. We maintain a website at www.flowcorp.com. The contents of our website are not incorporated into this prospectus.

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The Offering

Common Stock offered by the Selling Shareholders	7,183,018 Shares(1)
Offering	The Selling Shareholders may offer their shares from time to time through one or more underwriters, brokers or dealers, on the NASDAQ Stock National Market at market prices prevailing at the time of sale, in one or more negotiated transactions at prices acceptable to the Selling Shareholders or in private transactions.
Use of Proceeds	The proceeds from the sale of the shares covered by this prospectus will be received by the Selling Shareholders. We will not receive any of the proceeds from the sales by the Selling Shareholders of the shares covered by this prospectus.
Nasdaq National Market symbol	FLOW
Risk Factors	See Risk Factors beginning on page 7 for a discussion of factors that you should consider carefully before deciding to purchase our common stock.
Offering-related Information	On March 21, 2005, in a Private Investment in Public Equity Transaction (PIPE Transaction), we sold 17,473,116 equity units at $3.72 per unit for gross proceeds of $65 million, and net proceeds of $59.3 million. A unit consists of one share of our common stock and one warrant to buy 1/10th of a share of our common stock. Ten warrants give the holder the right to purchase one share of common stock for $4.07. The exercise price of the warrants was a negotiated price. On April 28, 2006, we converted, on a mandatory basis, all remaining common stock warrants (other than the warrants held by Third Point LLC, which could not be converted because doing so would have triggered the Company s poison pill) issued in connection with the PIPE Transaction to common stock. The warrant holders had the option of completing the conversion on a cash or cashless basis. All but 403,300 warrants were exercised and 1,220,497 shares of common stock were issued in exchange for $3.6 million. Proceeds of the PIPE were used to pay down existing debt of $59.3 million, including all of our subordinated debt. Under the terms of warrants previously issued to our senior and subordinated lenders, we are obligated to issue additional warrants if shares of our common stock are issued for prices less than market price. Because the issuance price of the common stock of the PIPE Transaction ($3.70) was less than market price ($4.28), we issued approximately 304,000 anti-dilution $0.01 warrants to our lenders. These warrants had a Black-Scholes value of approximately $1.7 million. All of the warrants issued to our senior and subordinated lenders have been exercised.

(1) Includes 403,300 shares of common stock issuable upon the exercise of outstanding warrants to purchase common stock.

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In connection with the PIPE Transaction, the Company entered into a Registration Rights Agreement (RRA). Under the RRA, the Company is required to keep the registration statement on Form S-1 for the resale of common stock issued in the PIPE Transaction and pursuant to warrants issued in the PIPE Transaction (PIPE Securities) effective and available for resale of PIPE Securities. The obligation exists until the earlier of five years, two years after the exercise of the warrants, or the resale of all PIPE Securities. If the registration is unavailable for resales for the period specified in the RRA, the Company will be obligated to pay, on a monthly basis, penalties to purchasers of PIPE Securities who still hold PIPE Securities. As of 2007, the monthly penalty would be approximately $600,000. The RRA originally provided that we would not have to pay penalties until the registration statement could not be used for resale for an aggregate total of 40 Trading Days. The registration statement has not been available for use since November 22, 2006. On January 24, 2007 (when the registration had not been available for resale for 40 Trading Days), the RRA was amended to increase the number of Trading Days to 102.

Historical Stock Price

Our stock is traded on the NASDAQ National Market under the symbol FLOW. The range of high and low sales prices for our common stock for the first, second, and third quarter of fiscal 2007 and the fourth quarter of fiscal 2007 through April 18, 2007 and the four quarters for fiscal 2006, 2005 and 2004 is set forth in the following table.

	Fiscal Year 2007		Fiscal Year 2006		Fiscal Year 2005		Fiscal Year 2004	
	High	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**
First Quarter	$ 16.74	$ 12.53	$ 7.83	$ 5.87	$ 3.66	$ 2.15	$ 1.94	$ 1.13
Second Quarter	14.68	10.60	9.39	6.83	3.55	2.70	3.11	1.36
Third Quarter	12.41	9.75	10.64	6.40	3.18	2.71	4.11	2.40
Fourth Quarter	12.97	10.45	14.30	9.06	6.60	2.85	3.74	2.20

We have not paid dividends to common shareholders in the past. Our Board of Directors intends to retain future earnings, if any, to finance development and expansion of our business and reduce debt and does not expect to declare dividends to common shareholders in the near future.

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Summary Financial Data

The following table provides summary historical financial data for the periods indicated. You should read this information in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our financial statements and the related notes included elsewhere in this prospectus.

The summary statement of operations data for each of the fiscal years ended April 30, 2006, 2005 and 2004 and the summary balance sheet data as of April 30, 2006 and 2005 are derived from our audited financial statements, which are included elsewhere in this prospectus. The summary statement of operations data for the fiscal year ended April 30, 2003 is derived from our audited financial statements, which are not included in this prospectus. The summary statement of operations data for the fiscal year ended April 30, 2002 and the summary balance sheet data as of April 30, 2003 and 2002 are derived from our unaudited financial statements which are not included in this prospectus. The summary statement of operations data for the nine months ended January 31, 2007 and the summary balance sheet data as of January 31, 2007 are derived from our unaudited financial statements which are included in this prospectus.

(In thousands, except per share amounts)	Nine Months Ended January 31, 2007 (unaudited)	Year Ended April 30, 2006 (restated)(1)	2005	2004	2003 (restated)(2)(3)	2002 (restated)(2)(3) (unaudited)
Statement of Operations Data:						
Sales	$ 163,851	$ 205,732	$ 172,966	$ 132,861	$ 121,833	$ 116,386
Income (Loss) Before Cumulative Effect of Change in Accounting Principle and Discontinued Operations	7,539	7,998	(12,174)	(10,668)	(43,965)	(7,966)
Net Income (Loss)	6,813	7,410	(21,197)	(11,274)	(67,813)	(8,024)
Basic Income (Loss) Per Share Before Cumulative Effect of Change in Accounting Principle and Discontinued Operations	0.20	0.23	(0.69)	(0.69)	(2.86)	(0.52)
Basic Earnings (Loss) Per Share	0.18	0.21	(1.19)	(0.73)	(4.42)	(0.53)
Diluted Income (Loss) Per Share Before Cumulative Effect of Change in Accounting Principle and Discontinued Operations	0.20	0.22	(0.69)	(0.69)	(2.86)	(0.52)
Diluted Income (Loss) Per Share	0.18	0.20	(1.19)	(0.73)	(4.42)	(0.53)

	January 31, 2007 (unaudited)	April 30, 2006 (restated)(1)	2005	2004	2003 (restated)(2)(3) (unaudited)	2002 (restated)(2)(3) (unaudited)
Balance Sheet Data:						
Working Capital	$ 47,760	$ 42,404	$ 6,154	$ (8,757)	$ (6,709)	$ 84,556
Total Assets	116,797	119,268	118,467	129,272	147,088	205,572
Short-Term Debt	1,870	3,247	13,443	48,727	61,056	5,237
Long-Term Obligations, net	2,810	3,774	5,704	38,081	29,023	83,453
Shareholders Equity (Deficit)	65,703	57,140	29,464	(8,217)	5,959	69,967

(1) As described in Note 2 to the April 30, 2006 Consolidated Financial Statements included elsewhere in this prospectus, we have restated our consolidated financial statements for the year ended April 30, 2006 to

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1) recognize additional revenue in the fourth quarter of the fiscal year 2006 for Nanojet machines sold by our Asia Waterjet segment, 2) reverse the incorrect accrual of installation costs for which installation had not yet occurred in our Asia Waterjet segment, 3) correct overstated freight and duty expenses associated with revenue transactions in our Asia Waterjet segment, 4) correct inventory-in-transit accounts between consolidated subsidiaries, 5) capitalize manufacturing variances at one of our subsidiaries in our North America Waterjet segment, 6) correct accounts payable by clearing items which had been paid but not appropriately recorded due to incomplete reconciliations in our North America Waterjet and Applications segments, and 7) correctly record a systems return in our North America Waterjet segment. Further, as described in Note 2 to the April 30, 2006 Consolidated Financial Statements included elsewhere in this prospectus, we have restated our consolidated financial statements for the year ended April 30, 2006 to 1) correct clerical errors in the compilation of total assets by reportable segments as of April 30, 2006 in Note 19 *Operating Segment and Geographical Information* to the Consolidated Financial Statements, and 2) appropriately present a receivable relating to the exercise of warrants and options as a noncash item rather than as a cash flow from financing activity.

(2) The Statement of Operations Data for years prior to fiscal 2003 and Balance Sheet Data prior to fiscal 2004 are unaudited and have been restated to reflect corrections to our consolidated income tax provisions and recording of minority interest. This restatement resulted in the following adjustments to the Statement of Operations Data for years prior to fiscal 2003 and Balance Sheet Data prior to fiscal 2004:

	2002		
	As previously reported	**As Restated**	**Reclassified for Discontinued Operations**
(Loss) Income Before Cumulative Effect of Change in Accounting Principle and Discontinued Operations	$ (8,244)	$ (8,415)	$ (7,966)
Net (Loss) Income	(7,853)	(8,024)	(8,024)
Net (Loss) Income per share:			
Basic & Diluted			
Net Loss	(0.52)	(0.53)	(0.53)

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	2003		2002	
	As previously reported	As Restated	As previously reported	As Restated
Balance Sheet Data:				
Working Capital	$ (6,709)	$ (6,709)	$ 84,532	$ 84,556
Total Assets	147,701	147,088	208,674	205,572
Total Shareholders Equity	4,872	5,959	71,054	69,967

(3) Our consolidated statements of operations for all periods have been recast to give effect to the sale of the Avure Business and present the results for the Avure Business as discontinued operations.

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RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the risks described below, together with the financial and other information contained in this prospectus, before making a decision to buy our common stock from the Selling Shareholder. If any of the following risks actually occur, our business, financial condition and results of operations could suffer. In these circumstances, the market price of our common stock could decline, and you may lose all or part of your investment in our common stock.

If we fail to remediate the material weaknesses and deficiencies in our internal control over financial reporting, we may be unable to accurately report our financial results or prevent fraud which could result in a loss of investor confidence in our financial reports and have an adverse effect on our business, our operating results, and our stock price.

Management has assessed the effectiveness of our internal control over financial reporting as of April 30, 2006, using the criteria described in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (or the COSO criteria). Based on its assessment of the design and related testing of our internal control over financial reporting, management has concluded that, as of April 30, 2006, we did not maintain effective internal control over financial reporting.

Based on the COSO criteria, management has identified certain control deficiencies that represent material weaknesses. A material weakness is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Specifically, the material weaknesses identified were:

- An insufficient complement of personnel with an appropriate level of accounting knowledge, experience and training in the application of generally accepted accounting principles (GAAP). As a result, we did not consistently maintain effective controls to ensure there was adequate (i) analysis, documentation, reconciliation and review of accounting records, and supporting data, and (ii) monitoring and oversight of the work performed by accounting and financial reporting personnel to ensure the accuracy and completeness of the consolidated financial statements in accordance with GAAP. This control deficiency resulted in errors and the restatement of our 2006 consolidated financial statements.

- A lack of adequate segregation of duties in certain locations.

- An aggregation of certain significant deficiencies related to revenue.

- An aggregation of certain significant deficiencies related to accounting for stock-based compensation.

- An aggregation of certain significant deficiencies related to tax accounting and financial statement disclosure.

- An ineffective control environment. As a result, we failed to institute all of the elements of an effective anti-fraud program and did not maintain controls adequate to prevent or detect instances of intentional override or intervention of our controls or intentional misconduct by certain former members of senior management in Flow Asia.

The material weaknesses in our internal control over financial reporting that we identified as of April 30, 2006, as well as our remediation efforts to date, are more fully discussed under Controls and Procedures on page 43 of this prospectus.

While we are taking steps to address the identified material weaknesses, there is no guarantee that these remediation steps will be sufficient to remediate the identified material weaknesses and control deficiencies or to prevent additional material weaknesses or control deficiencies.

We are experiencing significant growth in some of our markets, and if we are unable to respond, our business may suffer.

Interest in our products is growing rapidly and, in order to meet this demand we must continuously improve our efficiency and increase our capacity. We may need to change our processes or add or change personnel, equipment or facilities. If we are unable to successfully make these changes, we may not be able to sustain our growth rate and consequently lose market share.

We are experiencing increased competition in our markets, which may have an adverse effect on our financial results.

There are an increasing number of waterjet competitors entering our markets. If these new competitors are successful or if we are unable to respond to this competition, we may lose market share, our growth rate may slow, or our margins may suffer which may have an adverse effect on our financial results.

A significant portion of our new business has been derived from a few industries, and we could experience a reduction in the growth rate if conditions in one of those industries changed.

Although we serve many different industries and market segments, we have experienced strong growth in the aerospace and semi-conductor industries. A market slowdown in either industry, a postponement of a major project, such as occurred in aerospace, or a slowdown in the adoption of waterjet cutting in those industries could reduce revenue growth.

We are experiencing a decline in the domestic automotive industries, which may have an adverse effect on our financial results.

A portion of our revenues are derived from the domestic automotive industries, which are currently experiencing a decline in demand. The continued softness in these industries may have an adverse effect on our financial results.

Economic weakness in our served markets may adversely affect our financial results.

The products we sell are capital goods with individual system prices ranging from $60,000 to several million dollars. Many of our customers depend on long term financing from a financial institution to purchase our equipment. Economic weakness in the capital goods market and /or a credit tightening by the banking industry could reduce our sales and accordingly affect our financial results.

If we are unable to finalize the upgrades to our information technology systems that are currently in process, our future success may be negatively impacted.

In order to maintain our leadership position in the market and efficiently process increased business volume, we are making an $11 million, 2 year upgrade to our computer hardware, software and our Enterprise Resource Planning (ERP) system. Should we be unable to continue to fund this upgrade, or should the ERP system upgrade be unsuccessful or take longer to implement than anticipated, our ability to grow the business and our financial results could be adversely impacted.

We may be subject to significant financial penalties if the registration statement for the resale of PIPE securities is not available for resales.

In connection with a March 2005 Private Investment Public Equity transaction (PIPE Transaction) in which we sold $65 million of stock and warrants to investors, we entered into a Registration Rights Agreement (RRA). Under the RRA, we are required to keep the registration statement on Form S-1 for the resale of

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common stock issued in PIPE and pursuant to warrants issued in the PIPE (PIPE Securities) effective and available for resale of PIPE Securities. The obligation exists until the earlier of five years, two years after the exercise of the warrants, or the resale of all PIPE Securities. If the registration is unavailable for resales for the period specified in the RRA, we will be obligated to pay, on a monthly basis, penalties to purchasers of PIPE Securities who still hold PIPE Securities. As of the date of this prospectus, the monthly penalty would be approximately $600,000. The RRA originally provided that we would not have to pay penalties until the registration statement could not be used for resale for an aggregate total of 40 Trading Days. The registration statement has not been available for use since November 22, 2006. On January 24, 2007 (when the registration had not been available for resale for 40 Trading Days), the RRA was amended to increase the number of blackout days to 102. Until this post effective amendment is declared effective by the SEC, the number of Trading Days when the registration statement has not been available for resales will continue to increase. We will be obligated to file additional post-effective amendments in the future on an annual basis to include updating information and to reflect fundamental changes, if any occur. Depending on the timing of the filing of the post-effective amendments and how long it takes the SEC to declare such post-effective amendments effective, the registration statement may not be available for resales for periods of time.

Changes in the tax and regulatory rules or requirements in the countries in which we operate could impact our operations.

We have offices in 14 countries and have manufacturing facilities in three of those countries. Changes in the local tax or regulatory rules could reduce our ability to ship our products cross-border profitably or operate our local businesses cost effectively, which could adversely impact our financial results.

Our Chief Executive Officer has announced his intent to retire from the Company, and our ability to recruit a replacement Chief Executive Officer may negatively impact our future success.

On February 2, 2007, our Chief Executive Officer, Mr. Stephen Light, announced his intention to retire from the Company effective upon the appointment of a successor Chief Executive Officer. The Company has retained the services of executive search firm Korn/Ferry International and a search for his replacement is currently underway. We may encounter difficulties recruiting a suitable replacement for Mr. Light. We will need to conduct an extensive national search to select a qualified candidate, and may incur significant costs in locating and attracting a suitable replacement. If we are unable to recruit a suitable replacement Chief Executive Officer, or if the process takes longer than expected, our future success may be negatively impacted.

If we are unable to retain the current members of our senior management team and other key personnel or to recruit additional key personnel, our future success may be negatively impacted.

Besides Mr. Light s retirement discussed above, we may lose other key management personnel and encounter difficulties replacing these positions. We may also encounter difficulties in recruiting additional key personnel as our business grows. We may incur greater costs to attract replacement or additional personnel.

Our inability to protect our intellectual property rights, or our possible infringement on the proprietary rights of others, and related litigation could be time consuming and costly.

We defend our intellectual property rights because unauthorized copying and sale of our proprietary equipment and consumables represents a potential loss of revenue to us. From time to time we also receive notices from others claiming we infringe their intellectual property rights. The number of these claims may grow in the future, and responding to these claims may require us to stop selling or to redesign affected products, or to pay damages. On November 18, 2004, Omax Corporation (Omax) filed suit against us alleging that our products infringe Omax s patents. The suit also seeks to have a specific patent we hold declared invalid. Although the suit seeks damages of over $100 million, we believe Omax s claims are without merit and we are contesting Omax s allegations of infringement and also vigorously pursuing our claims against Omax with regard

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to our own patent. The outcome of this case is uncertain, and an unfavorable outcome is possible. We have and may continue to spend substantial amounts contesting Omax s claims and pursuing our own. See Note 14 to Consolidated Financial Statements for further discussion of contingencies.

Our inability to settle our current insurance coverage litigation related to a June, 2002 claim could be time consuming and costly.

In litigation arising out of a June 2002 incident, our excess insurance carrier notified us in December 2006 that it is contesting its obligation to provide coverage. As discussed in Note 14 to the Condensed Consolidated Financial Statements in Form 10-Q for the quarter ended January 31, 2007, we purchase product liability insurance to cover claims of this nature. We believe the carrier s position is without merit and we have commenced a declaratory judgment action seeking a determination that the carrier is obligated to provide a full defense of us. The outcome of this case is uncertain, and an unfavorable outcome is possible. We have not provided any loss accrual related to this matter as of January 31, 2007. The unresolved claims relating to this incident total approximately $7 million. We have and may continue to spend substantial amounts contesting the insurance carrier s denial of coverage.

Fluctuations in our quarterly operating results may cause our stock price to decline.

In the past, our operating results have fluctuated significantly from quarter to quarter and we expect them to continue to do so in the future due to a variety of factors, many of which are outside of our control. Our operating results may in some future quarter fall below the expectations of securities analysts and investors. In this event, the trading price of our common stock could decline significantly. In addition to the risks disclosed elsewhere in this prospectus, factors outside of our control that have caused our quarterly operating results to fluctuate in the past and that may affect us in the future include:

fluctuations in general economic conditions;

demand for UHP pumps and UHP water management systems generally;

fluctuations in the capital budgets of customers; and

development of superior products and services by our competitors.

In addition, factors within our control, such as our ability to deliver equipment in a timely fashion, have caused our operating results to fluctuate in the past and may affect us similarly in the future.

The factors listed above may affect both our quarter-to-quarter operating results as well as our long-term success. Given the fluctuations in our operating results, investors should not rely on quarter-to-quarter comparisons of our results of operations as an indication of our future performance or to determine any trend in our performance. Fluctuations in our quarterly operating results could cause the market price of and demand for our common stock to fluctuate substantially.

We do business in industries that are cyclical, which may result in weakness in demand for our products.

Our products are sold in many industries, including job shops, automotive and aerospace, that are highly cyclical. The machine tool industry, from 1998 through 2003, experienced a significant decline in global demand. Cyclical weaknesses in the industries that we serve could lead to a reduced demand for our products.

We may be affected by rising costs or lack of availability of materials, which could negatively impact our operations.

We have experienced and may continue to experience (i) significant increases in the costs, and (ii) shortages of materials we use in the manufacture of our products, such as steel, and we may not be able to either achieve

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corresponding increases in the prices of our products or reduce manufacturing costs to offset these increases, or if we do increase prices, we may experience lower sales. We have experienced and may continue to experience longer lead times for certain materials we use in the manufacture of our products, such as steel, and we may not be able to deliver our products in a timely fashion which could lower our sales. Any of the foregoing may adversely affect our financial results.

Our waterjet manufacturing capacity is concentrated within three locations and our ability to provide product to our customers would be impacted should one of the facilities be closed.

We operate three main manufacturing facilities to cover the worldwide production of our waterjet equipment: two in the United States, and one in Taiwan. Should any of these facilities suffer damages caused by an act of nature or terrorism, our ability to provide products to our customers in a timely manner would be affected for a period of time, which may have a negative impact on our operating results.

If we cannot develop technological improvements to our products through continued research and engineering, our financial results may be adversely affected.

In order to maintain our position in the market, we need to continue investment in research and engineering to improve our products and technologies and introduce new products and technologies. If we are unable to make such investment, if our research and engineering efforts do not lead to new and/or improved products or technologies, or if we experience delays in the development or acceptance of new and/or improved products, our financial results could be adversely affected.

We have outstanding options and stock units that have the potential to dilute the return of our existing common shareholders and cause the price of our common stock to decline.

We have granted stock options to our employees and other individuals. At January 31, 2007, we had options outstanding to purchase 1,077,604 shares of our common stock, at a weighted average exercise price of $8.95 per share. In addition, we have compensation plans with certain employees and have granted those employees common stock or stock units totaling 259,250 for the nine months ended January 31, 2007.

Washington law and our charter documents may make an acquisition of us more difficult.

Provisions in Washington law and in our articles of incorporation, bylaws, and rights plan could make it more difficult for a third-party to acquire us, even if doing so would benefit our shareholders. These provisions:

- *Establish a classified board of directors so that not all members of our board are elected at one time;*

- *Authorize the issuance of blank check preferred stock that could be issued by our board of directors (without shareholder approval) to increase the number of outstanding shares (including shares with special voting rights), each of which could hinder a takeover attempt;*

- *Provide for a Preferred Share Rights Purchase Plan or poison pill;*

- *Impose restrictions on certain transactions between a corporation and certain significant shareholders.*

- *Provide that directors may be removed only at a special meeting of shareholders and provide that only directors may call a special meeting;*

- *Require the affirmative approval of a merger, share exchange or sale of substantially all of the Corporation s assets by 2/3 of the Corporation s shares entitled to vote; and*

Provide for 60 day advance notification for shareholder proposals and nominations at shareholder meetings.

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Our largest shareholder, Third Point LLC, has made requests and demands that could require the focus of the Board of Directors and Management.

Our largest shareholder, Third Point LLC (Third Point) has urged the Company to halt the search for a replacement Chief Executive Officer, and to retain an investment bank for the purpose of offering the Company for sale (subsequently changed to a demand to &