MAGNETEK, INC.
Form 10-Q
February 09, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: December 31, 2006

OR

o **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 1-10233

MAGNETEK, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE	**95-3917584**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

N49 W13650 Campbell Drive
Menomonee Falls, Wisconsin 53051
(Address of principal executive offices)

(262) 783-3500
(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 x No o

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o

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

Yes o No x

The number of shares outstanding of Registrant s Common Stock, as of January 31, 2007, was 29,838,345 shares.

2007 MAGNETEK FORM 10-Q

TABLE OF CONTENTS FOR THE QUARTERLY REPORT ON FORM 10Q
FOR THE FISCAL QUARTER ENDED DECEMBER 31, 2006

MAGNETEK, INC.

Part I. **Financial Information**

Item 1. Financial Statements
Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations
Item 3. Quantitative and Qualitative Disclosures about Market Risk
Item 4. Controls and Procedures

Part II. **Other Information**

Item 1. Legal Proceedings
Item 1A. Risk Factors
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
Item 3. Defaults upon Senior Securities
Item 4. Submission of Matters to a Vote of Security Holders
Item 5. Other Information
Item 6. Exhibits

Signatures

PART I. FINANCIAL INFORMATION

Item 1 Financial Statements

MAGNETEK, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands, except per share data, unaudited)

	Three Months Ended (13 Weeks) December 31, 2006	(13 Weeks) January 1, 2006
Net sales	$ 27,578	$ 26,063
Cost of sales	20,519	18,136
Gross profit	7,059	7,927
Operating expenses:		
Research and development	1,588	1,310
Selling, general and administrative	9,189	7,125
Loss from operations	(3,718)	(508)
Non operating expense (income):		
Interest expense	1,057	808
Interest income	(905)	(106)
Other expense	325	
Loss from continuing operations before provision for income taxes	(4,195)	(1,210)
Provision for income taxes	373	345
Loss from continuing operations	(4,568)	(1,555)
Loss from discontinued operations, net of tax	(1,647)	(170)
Net loss	$ (6,215)	$ (1,725)
Loss per common share		
Basic and diluted:		
Loss from continuing operations	$ (0.16)	$ (0.05)
Loss from discontinued operations	$ (0.06)	$ (0.01)
Net loss	$ (0.21)	$ (0.06)
Weighted average shares outstanding:		
Basic	29,264	28,890
Diluted	29,264	28,890

See accompanying notes

MAGNETEK, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands, except per share data, unaudited)

	Six Months Ended (26 Weeks) December 31, 2006	(26 Weeks) January 1, 2006
Net sales	$ 53,533	$ 49,676
Cost of sales	39,054	34,463
Gross profit	14,479	15,213
Operating expenses:		
Research and development	2,807	2,479
Selling, general and administrative	16,586	13,740
Loss from operations	(4,914)	(1,006)
Non operating expense (income):		
Interest expense	2,133	1,261
Interest income	(1,193)	(132)
Other expense	325	
Loss from continuing operations before provision for income taxes	(6,179)	(2,135)
Provision for income taxes	649	679
Loss from continuing operations	(6,828)	(2,814)
Income (loss) from discontinued operations, net of tax	(2,581)	35
Net loss	$ (9,409)	$ (2,779)
Earnings (loss) per common share		
Basic and diluted:		
Loss from continuing operations	$ (0.23)	$ (0.10)
Income (loss) from discontinued operations	$ (0.09)	$ 0.00
Net loss	$ (0.32)	$ (0.10)
Weighted average shares outstanding:		
Basic	29,138	28,888
Diluted	29,138	29,273

MAGNETEK, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Amounts in thousands)

	December 31, 2006 (Unaudited)	July 2, 2006
ASSETS		
Current assets:		
Cash	$ 7,276	$ 96
Restricted cash	22,602	22,602
Accounts receivable, net	17,578	14,765
Inventories	12,676	13,134
Prepaid expenses and other current assets	1,016	693
Assets held for sale		140,549
Total current assets	61,148	191,839
Property, plant and equipment	18,836	18,580
Less-accumulated depreciation	15,141	14,369
Net property, plant and equipment	3,695	4,211
Goodwill	28,117	28,150
Other assets	7,809	8,826
Total Assets	$ 100,769	$ 233,026
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 9,831	$ 7,862
Accrued liabilities	12,240	8,663
Accrued arbitration award	22,602	22,602
Liabilities held for sale		75,933
Current portion of long-term debt		27,412
Total current liabilities	44,673	142,472
Long-term debt, net of current portion	37	43
Pension benefit obligations, net	25,827	45,494
Deferred income taxes	2,559	2,109
Commitments and contingencies		
Stockholders equity		
Common stock	293	287
Paid in capital in excess of par value	132,459	129,473
Accumulated deficit	(16,240)	(6,831)
Accumulated other comprehensive loss	(88,839)	(80,021)
Total stockholders equity	27,673	42,908
Total Liabilities and Stockholders Equity	$ 100,769	233,026

See accompanying notes

MAGNETEK, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOW
(Amounts in thousands, unaudited)

	Six Months Ended (26 Weeks) December 31, 2006	(26 Weeks) January 1, 2006
Cash flows from continuing operating activities:		
Loss from continuing operations	$ (6,828)	$ (2,814)
Adjustments to reconcile loss from continuing operations to net cash used in operating activities:		
Depreciation and amortization	1,056	1,125
Write-off of deferred financing	670	
Stock based compensation expense	1,314	222
Changes in operating assets and liabilities	(194)	1,288
Cash contribution to pension fund	(30,000)	
Total adjustments	(27,154)	2,635
Net cash used in continuing operating activities	(33,982)	(179)
Cash flows from discontinued operations:		
Income (loss) from discontinued operations	(2,581)	35
Adjustments to reconcile (income) loss from discontinued operations to net cash provided by discontinued operations:		
Depreciation and amortization		3,364
Changes in operating assets and liabilities	5,189	1,332
Capital expenditures	(930)	(2,763)
Net cash provided by discontinued operations	1,678	1,968
Net cash provided by (used in) operating activities	(32,304)	1,789
Cash flows from investing activities:		
Proceeds from sale of business, net of transaction costs	65,823	
Deposit into escrow account		(22,602)
Capital expenditures	(275)	(422)
Net cash provided by (used in) investing activities	65,548	(23,024)
Cash flow from financing activities:		
Proceeds from issuance of common stock	1,561	149
Borrowings under long term notes		18,000
Repayment of long term notes	(18,000)	
Borrowings (repayments) under line-of-credit agreements	(9,412)	4,234
Principal payments under capital lease obligations	(6)	(6)
Increase in deferred financing costs	(207)	(1,468)
Net cash provided by (used in) financing activities	(26,064)	20,909
Net increase (decrease) in cash	7,180	(326)
Cash at the beginning of the period	96	595
Cash at the end of the period	$ 7,276	$ 269

See accompanying notes

MAGNETEK, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006
(Amounts in thousands unless otherwise noted, except per share data, unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Magnetek, Inc. and its subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial reporting and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in the Company s Form 10-K for the year ended July 2, 2006 filed with the Securities and Exchange Commission. In the Company s opinion, these unaudited statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial position of the Company as of December 31, 2006, and the results of its operations and its cash flows for the three- and six-months then ended. Results for the three- and six-months ended December 31, 2006 are not necessarily indicative of results that may be experienced for the full fiscal year.

The Company uses a fifty-two, fifty-three week fiscal year ending on the Sunday nearest to June 30. Fiscal quarters are the thirteen or fourteen week periods ending on the Sunday nearest September 30, December 31, March 31 and June 30. The three- and six-month periods ended December 31, 2006 and January 1, 2006 each contained 13 and 26 weeks respectively.

Use of Estimates - The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Significant areas requiring management estimates include the following key financial areas:

Accounts Receivable

Accounts receivable represent receivables from customers in the ordinary course of business. The Company is subject to losses from uncollectible receivables in excess of its allowances. The Company maintains allowances for doubtful accounts for estimated losses from customers inability to make required payments. In order to estimate the appropriate level of this allowance, the Company analyzes historical bad debts, customer concentrations, current customer creditworthiness, current economic trends and changes in customer payment patterns. If the financial conditions of the Company s customers were to deteriorate and to impair their ability to make payments, additional allowances may be required in future periods. The Company s management believes that all appropriate allowances have been provided.

Inventories

The Company s inventories are stated at the lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method, including material, labor and factory overhead. Inventory on hand may exceed future demand either because the product is obsolete, or the amount on hand is more than can be used to meet future needs. The Company identifies potentially obsolete and excess inventory by evaluating overall inventory levels. In assessing the ultimate realization of inventories, the Company is required to make judgments as to future demand requirements and compare those with the current or committed inventory levels. If future demand requirements are less favorable than those projected by management, additional inventory write-downs may be required.

Reserves for Contingencies

The Company periodically records the estimated impacts of various conditions, situations or circumstances involving uncertain outcomes. The accounting for such events is prescribed under Statement of Financial Accounting Standard (SFAS) No. 5, *Accounting for Contingencies*. SFAS No. 5 defines a contingency as an existing condition, situation, or

7

set of circumstances involving uncertainty as to possible gain or loss to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur.

SFAS No. 5 does not permit the accrual of gain contingencies under any circumstances. For loss contingencies, the loss must be accrued if (1) information is available that indicates it is probable that the loss has been incurred, given the likelihood of uncertain events; and (2) that the amount of the loss can be reasonably estimated.

The accrual of a contingency involves considerable judgment on the part of management. The Company uses its internal expertise, and outside experts, as necessary, to help estimate the probability that a loss has been incurred and the amount or range of the loss.

Income Taxes

The Company uses the liability method to account for income taxes. The preparation of consolidated financial statements involves estimating the Company s current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in the condensed consolidated balance sheets. An assessment of the recoverability of the deferred tax assets is made, and a valuation allowance is established based upon this assessment.

Pension Benefits

The valuation of the Company s pension plan requires the use of assumptions and estimates to develop actuarial valuations of expenses, assets and liabilities. These assumptions include discount rates, investment returns and mortality rates. Changes in assumptions and future investments returns could potentially have a material impact on the Company s expenses and related funding requirements.

Revenue Recognition The Company s policy is to recognize revenue when the earnings process is complete. The criteria used in making this determination are persuasive evidence that an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility is reasonably assured. Sales are recorded net of returns and allowances, which are estimated using historical data at the time of sale.

Stock-Based Compensation The Company accounts for all stock-based compensation in accordance with SFAS No. 123 (R), *Share-Based Payment*, which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the Company s financial statements based upon their fair values. The Company adopted SFAS No. 123 in July, 2005 (fiscal year 2006) and selected the modified prospective method of adoption in which compensation cost is recognized beginning with the effective date. In accordance with the modified prospective method of adoption, the Company s results of operations for periods prior to adoption were not restated.

Property, Plant and Equipment Additions and improvements are capitalized at cost, whereas expenditures for maintenance and repair are charged to expense as incurred. Depreciation is provided over the estimated useful lives of the respective assets principally on the straight-line method (machinery and equipment normally five to ten years, buildings and improvements normally ten to forty years).

Goodwill In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, the Company reviews the carrying value of goodwill at least annually, and more frequently if indicators of potential impairment arise, using discounted future cash flow analysis as prescribed in SFAS No. 142.

Deferred Financing Costs Costs incurred to obtain financing are deferred and included in other assets in the condensed consolidated balance sheets. Deferred financing costs are amortized over the term of the financing facility and these expenses are included in interest expense in the accompanying condensed consolidated statements of operations.

Warranties The Company offers warranties for certain products that it manufactures, with the warranty term generally ranging from one to two years. Warranty reserves are established for costs expected to be incurred after the sale and delivery of products under warranty, based mainly on known product failures and historical experience. Actual repair costs incurred for products under warranty are charged against the established reserve balance as incurred.

Earnings per Share In accordance with SFAS No. 128, *Earnings per Share*, basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share incorporate the incremental shares issuable upon the assumed exercise of stock options as if all exercises had occurred at the beginning of the fiscal period.

Recent Accounting Pronouncements In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections.* SFAS No. 154 replaces APB No. 20, *Accounting Changes*, and SFAS No. 3, *Reporting Accounting Changes*

---

in Interim Financial Statements, and establishes retrospective application as the required method for reporting a change in accounting principle. SFAS No. 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. The reporting of a correction of an error by restating previously issued financial statements is also addressed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of this pronouncement on July 3, 2006, did not have a material effect on the Company s financial position, results of operations or liquidity.

In July 2006, the FASB issued FASB Interpretation No. 48 (FIN 48) Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109 which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN 48 provides guidance on derecognition, classification, accounting in interim periods, and disclosure requirements for uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006. The adoption of this pronouncement is not expected to have a material effect on the Company s financial position, results of operations, or liquidity.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin 108, Considering the Effects on Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements, (SAB 108). SAB 108 requires registrants to quantify errors using both the income statement method (i.e. iron curtain method) and the rollover method and requires adjustment if either method indicates a material error. If a correction in the current year relating to prior year errors is material to the current year, then the prior year financial information needs to be corrected. A correction to the prior year results that are not material to those years would not require a restatement process where prior financials would be amended. SAB 108 is effective for fiscal years ending after November 15, 2006. The Company does not anticipate that SAB 108 will have a material effect on the Company s consolidated financial statements.

<u>Derivative Financial Instruments</u> The Company periodically uses derivative financial instruments to reduce financial market risks. These instruments are used to hedge foreign currency and interest rate market exposures. The Company does not use derivative financial instruments for speculative or trading purposes. The accounting policies for these instruments are based on the Company s designation of such instruments as hedging transactions. The criteria the Company uses for designating an instrument as a hedge include the instrument s effectiveness in risk reduction and the matching of the derivative to the underlying transaction. The resulting gains or losses are accounted for as part of the transactions being hedged, except that losses not expected to be recovered upon the completion of the hedge transaction are expensed. The Company s continuing operations had no derivative financial instruments at December 31, 2006 and July 2, 2006.

<u>Foreign Currency Translation</u> The Company s foreign entities accounts are measured using local currency as the functional currency. Assets and liabilities are translated at the exchange rate in effect at the end of the period. Revenues and expenses are translated at the rates of exchange prevailing during the period. Unrealized translation gains and losses arising from differences in exchange rates from period to period are included as a component of accumulated other comprehensive loss in stockholders equity.

<u>Reclassifications</u> Certain prior year balances were reclassified to conform to the current year presentation.

2. **<u>Discontinued Operations</u>**

The Company s power electronics business as well as certain expenses incurred related to businesses the Company no longer owns are classified as discontinued operations. The results of discontinued operations are as follows:

	Three Months Ended December 31, 2006	January 1, 2006	Six Months Ended December 31, 2006	January 1, 2006
Net sales	$ 10,056	$ 37,532	$ 53,545	$ 73,960
	$ (1,294)	$ 538	$ (1,629)	$ 1,654

Income (loss) from discontinued operations before interest and income taxes				
Interest expense, net	247	303	521	598
Provision for income taxes	106	405	431	1,021
Income (loss) from discontinued operations	$ (1,647)	$ (170)	$ (2,581)	$ 35

9

Income (loss) from discontinued operations in the table above includes charges of $280 and $310 for the three- and six-month periods ended December 31, 2006 respectively, and $907 and $1,319 for the three- and six-month periods ended January 1, 2006, for legal fees and costs related to the Nilssen patent infringement claim (see Note 5 of Notes to Condensed Consolidated Financial Statements), environmental issues, and asbestos claims related to businesses that the Company no longer owns.

During the fourth quarter of fiscal year 2006, the Company committed to a plan to divest its power electronics business. As a result, in June 2006, the Company reclassified the assets and liabilities as held for sale and the results of this business as discontinued operations. The Company s power electronics business was comprised mainly of the Company s wholly-owned subsidiaries Magnetek S.p.A. (Italy), Magnetek Kft. (Hungary) and Magnetek Electronics Co., Ltd. (China), and a North American division located in Chatsworth, California. The Company entered into an agreement to sell the business to Power-One, Inc. (see Note 13 of Notes to Condensed Consolidated Financial Statements), and the transaction was completed on October 23, 2006.

The results of the Company s power electronics business are as follows:

	Three Months Ended December 31, 2006	**January 1, 2006**	**Six Months Ended December 31, 2006**	**January 1, 2006**
Net sales	$ 10,056	$ 37,532	$ 53,545	$ 73,960
Income (loss) from discontinued operations before interest and income taxes	$ (1,014)	$ 1,445	$ (1,319)	$ 2,973
Interest expense, net	247	303	521	598
Provision for income taxes	106	405	431	1,021
Income (loss) from discontinued operations - power electronics business	$ (1,367)	$ 737	$ (2,271)	$ 1,354

Assets and liabilities of the Company s power electronics business classified as held for sale as of July 2, 2006, were as follows:

Assets and Liabilities of Discontinued Power Electronics Business	**July 2, 2006**
Cash and equivalents	$ 1,491
Accounts receivable	51,431
Inventories	45,438
Net property, plant and equipment	27,320
Other assets	18,485
Assets of discontinued power electronics business	$ 144,165
Eliminations	(3,616)
Total assets	$ 140,549
Accounts payable	$ 34,985
Other current liabilities	5,926
Other long term liabilities	10,728
Long term debt	24,294
Liabilities of discontinued power electronics business	$ 75,933

During fiscal year 2005, the Company committed to a plan to divest its telecom power business, and as a result, reclassified assets and liabilities as held for sale and the results of the business as discontinued operations. The Company did not complete the divestiture of its telecom power business despite actively marketing the business to potential interested parties at a reasonable price. In October 2006, the Company decided to retain the business, and accordingly, the operating results

of its telecom power business have been classified as continuing operations in the accompanying consolidated statements of operations and its assets and liabilities have been reclassified from held for sale to held and used in the accompanying consolidated balance sheets for all periods presented.

The results of the Company s telecom power business are as follows:

	Three Months Ended December 31, 2006	January 1, 2006	Six Months Ended December 31, 2006	January 1, 2006
Net sales	$ 4,580	$ 4,262	$ 8,021	$ 7,792
Loss from telecom power business	$ (475)	$ (142)	$ (1,105)	$ (134)

No interest expense or provision for income tax was allocated to the Company s telecom power business for either of the periods presented above.

3. Stock-Based Compensation

The Company has two stock option plans (the Plans), one of which provides for the issuance of both incentive stock options (under Section 422A of the Internal Revenue Code of 1986) and non-qualified stock options at exercise prices not less than the fair market value at the date of grant, and one of which only provides for the issuance of non-qualified stock options at exercise prices not less than the fair market value at the date of grant. One of the Plans also provides for the issuance of stock appreciation rights, restricted stock, incentive bonuses and incentive stock units. The total number of shares of the Company s common stock authorized to be issued upon exercise of the stock options and other stock rights under the Plans is 2,100,000. Options granted under these Plans vest in equal annual installments of two, three or four years.

Effective July 4, 2005, the Company adopted SFAS No. 123 (R), *Share-Based Payment*, which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the Company s financial statements based upon their fair values. The Company selected the modified prospective method of adoption in which compensation cost is recognized beginning with the effective date. In accordance with the modified prospective method of adoption, the Company s results of operations for prior periods were not restated.

In the fourth quarter of fiscal 2005, the Company approved the acceleration of the vesting of underwater unvested stock options held by the Company s current employees, including executive officers, on June 1, 2005. No stock options held by directors were subject to the acceleration. The decision to accelerate vesting of these underwater options was made primarily to avoid recognizing compensation cost in the consolidated statement of operations upon adoption of SFAS No. 123 (R), as described above. As a result of the acceleration, the Company reduced the stock option compensation expense it otherwise would be required to record by approximately $1.9 million in fiscal 2006, $1.4 million in fiscal 2007 and less than $0.1 million in fiscal 2008 on a pre-tax basis, resulting in an additional $3.4 million of pro-forma expense in fiscal 2005. The accelerated vesting was a modification of outstanding awards as defined by FAS 123, which resulted in incremental pro-forma compensation expense of $0.3 million in fiscal 2005.

The Company did not issue any stock options in the six month period ended December 31, 2006.

In August 2005, the Company granted 500,000 shares of restricted stock (the August 2005 stock grant) with a fair value of $2.77 per share to certain officers and key employees. The restricted shares fully vest on January 1, 2009. The total estimated compensation expense related to the grant of $1.4 million is being recorded ratably from the grant date through the vesting date. The divestiture of the Company s power electronics business in October 2006 resulted in the forfeiture of 90,000 shares of the August 2005 stock grant that were granted to employees of the business, which reduced stock compensation expense by $82 for the three- and six-month periods ended December 31, 2006. Subsequent to the divestiture, the Company announced the relocation of its corporate offices from Chatsworth, California to Menomonee Falls, Wisconsin, which resulted in the termination of several corporate officers. The Company accelerated the vesting of 175,000 shares of the August 2005 stock grant that were granted to these officers which increased stock compensation expense by $218 for the three- and six-month periods ended December 31, 2006. Total net compensation expense related to the August 2005 stock grant in the three-month period ended December 31, 2006 was $184. As of December 31, 2006, there was approximately $0.4 million of total unrecognized compensation cost related to the grant, to be amortized ratably over a weighted-average period of 2.0 years.

11

In July 2006, the Company granted a bonus equal to 200,000 shares of stock to its former CEO who elected to defer the shares pursuant to the terms of the Director Compensation and Deferral Investment Plan (DDIP) pending approval of an amendment to the DDIP by the Company s shareholders. Such amendment was approved at the annual meeting of the shareholders on October 25, 2006. Accordingly, the Company recorded compensation expense of $952 related to the bonus in the three-month period ended December 31, 2006.

Compensation expense related to all stock-based awards for the three- and six-month periods ended December 31, 2006 was as follows:

	December 31, 2006 Three months ended	Six months ended
Bonus to the Company s former CEO	$ 952	$ 952
August 2005 restricted stock grant	184	287
Director stock options	52	75
	$ 1,188	$ 1,314

4. **Inventories**

Inventories at December 31, 2006 and July 2, 2006 consist of the following:

	December 31, 2006	July 2, 2006
Raw materials and stock parts	$ 9,632	$ 10,210
Work-in-process	1,636	1,637
Finished goods	1,408	1,287
	$ 12,676	$ 13,134

5. **Commitments and Contingencies**

Litigation Product Liability

The Company has settled or otherwise resolved all of the product liability lawsuits associated with its discontinued business operations. The last remaining limited obligation to defend and indemnify the purchaser of a discontinued business operation against new product liability claims expired in December 2003 and the Company believes that any new claims would either qualify as an assumed liability, as defined in the various purchase agreements, or would be barred by an applicable statute of limitations. The Company is also a named party in two product liability lawsuits related to the Telemotive Industrial Controls business acquired in December 2002 through the purchase of the stock of MXT Holdings, Inc. Both claims were tendered to the insurance companies that provided coverage for MXT Holdings, Inc., against such claims and the defense and indemnification has been accepted by the carriers, subject to a reservation of rights. Management believes that the insurers will bear all liability, if any, with respect to both cases and that the proceedings, individually or in the aggregate, will not have a material adverse effect on the Company s results of operations or financial position.

In August 2006, Pamela L. Carney, Administrator of the Estate of Michael J. Carney, filed a lawsuit in the Court of Common Pleas of Westmoreland County, Pennsylvania, against the Company and other defendants, alleging that a product manufactured by the Telemotive Industrial Controls business acquired by the Company in December 2002 contributed to an accident that resulted in the death of Michael J. Carney in August 2004. The claim has been tendered to the Company s insurance carrier and legal counsel has been retained to represent the Company. Plaintiff s claim for damages is unknown at this time, but management believes that the Company s insurer will bear all liability for the claim, if any.

The Company has been named, along with multiple other defendants, in asbestos-related lawsuits associated with business operations previously acquired by the Company, but which are no longer owned. During the Company s ownership, none of the businesses produced or sold asbestos-containing products. With respect to these claims, the Company is either contractually indemnified against liability for asbestos-related claims or believes that it has no liability for such claims. The Company aggressively seeks dismissal from these proceedings, and has also tendered the defense of these cases to the

insurers of the previously acquired businesses and is awaiting their response. The Company has also filed a late claim in the amount of $2.5 million in the Federal-Mogul bankruptcy proceedings to recover attorney s fee paid for the defense of these claims, which the Company believes is an obligation of Federal Mogul although the claim is subject to challenge. Management does not believe the asbestos proceedings, individually or in the aggregate, will have a material adverse effect on its financial position or results of operations.

Litigation Patent Infringement

In April 1998, Ole K. Nilssen (Nilssen) filed a lawsuit in the U.S. District Court for the Northern District of Illinois alleging infringement by the Company of seven of his patents pertaining to electronic ballast technology, and seeking unspecified damages and injunctive relief to preclude the Company from making, using or selling products allegedly infringing his patents. The Company denied that its products infringed any valid patent and filed a response asserting affirmative defenses, as well as a counterclaim for a judicial declaration that its products do not infringe the patents asserted by Mr. Nilssen and also that the asserted patents are invalid. In June 2001, the Company sold its lighting business to Universal Lighting Technologies, Inc. (ULT), and agreed to provide a limited indemnification against certain claims of infringement that Nilssen might allege against ULT. In April 2003, Nilssen s lawsuit and the counterclaims were dismissed with prejudice and both parties agreed to submit limited issues in dispute to binding arbitration before an arbitrator with a relevant technical background. The arbitration occurred in November, 2004 and a decision awarding Nilssen $23.4 million was issued on May 3, 2005, to be paid within ten days of the award. Nilssen s counsel filed a motion to enter the award in U.S. District Court for the Northern District of Illinois, and Magnetek filed a counter-motion to vacate the award for a number of reasons, including that the award was fraudulently obtained. Magnetek s request for oral argument was granted and the hearing took place on October 19, 2005. A decision has not been announced. An unfavorable decision by the Court would likely result in payment of the award to Nilssen.

In February 2003, Nilssen filed a second lawsuit in the U.S. District Court for the Northern District of Illinois alleging infringement by ULT of twenty-nine of his patents pertaining to electronic ballast technology, and seeking unspecified damages and injunctive relief to preclude ULT from making, using or selling products allegedly infringing his patents. ULT made a claim for indemnification, which the Company accepted, subject to the limitations set forth in the sale agreement. The case is now pending in the Central District of Tennessee. Nilssen voluntarily dismissed all but four of the patents from the lawsuit. The Company denies that the products for which it has an indemnification obligation to ULT infringe any valid patent and responded on behalf of ULT asserting affirmative defenses, as well as a counterclaim for a judicial declaration that the patents are unenforceable and invalid and that the products do not infringe Nilssen s patents. ULT requested a re-examination of the patents at issue by the Patent and Trademark Office and the request was granted. Meanwhile, the case against ULT has been stayed pending Nilssen s appeal of an unfavorable decision against him in another case that could influence the outcome of his lawsuits against ULT. The Company will continue to aggressively defend the claims against ULT that are subject to defense and indemnification; however, an unfavorable decision could have a material adverse effect on the Company s financial position, cash flows and results of operations.

Environmental Matters - General

From time to time, Magnetek has taken action to bring certain facilities associated with previously owned businesses into compliance with applicable environmental laws and regulations. Upon the subsequent sale of certain businesses, the Company agreed to indemnify the buyers against environmental claims associated with the divested operations, subject to certain conditions and limitations. Remediation activities, including those related to the Company s indemnification obligations, did not involve material expenditures during the three and six months ended December 31, 2006 and January 1, 2006.

The Company has also been identified by the United States Environmental Protection Agency and certain state agencies as a potentially responsible party for cleanup costs associated with alleged past waste disposal practices at several previously owned facilities and offsite locations. Its remediation activities as a potentially responsible party were not material in the second quarter of fiscal years 2007 and 2006. Although the materiality of future expenditures for environmental activities may be affected by the level and type of contamination, the extent and nature of cleanup activities required by governmental authorities, the nature of the Company s alleged connection to the contaminated sites, the number and financial resources of other potentially responsible parties, the availability of indemnification rights against third parties and the identification of additional contaminated sites, the Company s estimated share of liability, if any, for environmental remediation, including its indemnification obligations, is not expected to be material.

Century Electric (McMinnville, Tennessee)

Prior to the Company s purchase of Century Electric, Inc. (Century Electric) in 1986, Century Electric acquired a business from Gould Inc. (Gould) in May 1983 that included a leasehold interest in a fractional horsepower electric motor manufacturing facility located in McMinnville, Tennessee. Gould agreed to indemnify Century Electric from and against liabilities and expenses arising out of the handling and cleanup of certain waste materials, including but not limited to cleaning up any polychlorinated biphenyls (PCBs) at the McMinnville facility (the 1983 Indemnity). The presence of PCBs and other substances, including solvents, in the soil and in the groundwater underlying the facility and in certain offsite soil, sediment and biota samples has been identified. The McMinnville plant is listed as a Tennessee Inactive Hazardous Waste Substance Site and plant employees were notified of the presence of contaminants at the facility. Gould has completed an interim remedial excavation and disposal of onsite soil containing PCBs and a preliminary investigation and cleanup of certain onsite and offsite contamination. The Company believes the cost of further investigation and remediation (including ancillary costs) is covered by the 1983 Indemnity. The Company sold its leasehold interest in the McMinnville plant in August 1999 and while the Company believes that Gould will continue to perform substantially under its indemnity obligations, Gould s substantial failure to perform such obligations could have a material adverse effect on the Company s financial position, cash flows and results of operations.

Effect of Fruit of the Loom Bankruptcy (Bridgeport, Connecticut)

In 1986, the Company acquired the stock of Universal Manufacturing Company (Universal) from a predecessor of Fruit of the Loom (FOL), and the predecessor agreed to indemnify the Company against certain environmental liabilities arising from pre-acquisition activities at a facility in Bridgeport, Connecticut. Environmental liabilities covered by the indemnification agreement include completion of additional cleanup activities, if any, at the Bridgeport facility (sold in connection with the sale of the transformer business in June 2001) and defense and indemnification against liability for potential response costs related to offsite disposal locations. FOL, the successor to Universal s indemnification obligation, filed a petition for Reorganization under Chapter 11 of the Bankruptcy Code in 1999 and the Company filed a proof of claim in the proceeding for obligations related to the environmental indemnification agreement. The Company believes that FOL had substantially completed the clean-up obligations required by the indemnification agreement prior to the bankruptcy filing. In November 2001, the Company and FOL entered into an agreement involving the allocation of certain potential tax benefits and Magnetek withdrew its claims in the bankruptcy proceeding. FOL s obligation to the state of Connecticut was not discharged in the reorganization proceeding. In October 2006, the owner of the Bridgeport facility filed a lawsuit in Superior Court, J.D. of Fairfield, Connecticut alleging that the Company is obligated to remediate environmental contamination at the facility. The Company has filed a Motion to Stay and Remand the matter to the Connecticut Department of Environmental Protection (DEP) on the basis that DEP has primary jurisdiction to determine the need and responsibility for any further remediation. FOL s inability to satisfy its remaining obligations related to the Bridgeport facility and any offsite disposal locations, or an unfavorable ruling in the lawsuit with the owner of the Bridgeport facility, or the discovery of additional environmental contamination at the Bridgeport facility could have a material adverse effect on the Company s financial position, cash flows or results of operations.

6. **Comprehensive Loss**

For the fiscal periods ended December 31, 2006 and January 1, 2006, comprehensive loss consisted of the following:

	Three Months Ended December 31, 2006	January 1, 2006	Six Months Ended December 31, 2006	January 1, 2006
Net loss	$ (6,215)	$ (1,725)	$ (9,409)	$ (2,779)
Currency translation adjustment	(161)	2	(177)	245
Comprehensive loss	$ (6,376)	$ (1,723)	$ (9,586)	$ (2,534)

7. **Earnings (Loss) Per Share**

The following table sets forth the computation of basic and diluted earnings (loss) per share for the three- and six-months ended December 31, 2006 and January 1, 2006:

14

	Three Months Ended December 31, 2006	January 1, 2006	Six Months Ended December 31, 2006	January 1, 2006
Numerator:				
Loss from continuing operations	$ (4,568)	$ (1,555)	$ (6,828)	$ (2,814)
Income (loss) from discontinued operations	(1,647)	(170)	(2,581)	35
Net loss	$ (6,215)	$ (1,725)	$ (9,409)	$ (2,779)
Denominator:				
Weighted average shares for basic earnings per share	29,264	28,890	29,138	28,888
Add dilutive effective of stock options outstanding				385
Weighted average shares for diluted earnings per share	29,264	28,890	29,138	29,273
Basic & Diluted:				
Loss per share from continuing operations	$ (0.16)	$ (0.05)	$ (0.23)	$ (0.10)
Earnings (loss) per share from discontinued operations	$ (0.06)	$ (0.01)	$ (0.09)	$ 0.00
Net loss per share	$ (0.21)	$ (0.06)	$ (0.32)	$ (0.10)

Due to the loss from continuing operations, the loss from discontinued operations, and the net loss for the three- and six-months ended December 31, 2006, the effect of 0.9 million shares and 0.8 million shares respectively of stock options outstanding was excluded from the calculation of diluted loss per share, as their impact would be anti-dilutive. Similarly, the dilutive effect of 0.5 million shares of stock options outstanding was not included in the calculation of diluted loss per share from continuing operations, loss per share from discontinued operations or net loss per share for the three-months ended January 1, 2006, as inclusion of these shares would be anti-dilutive; nor was the dilutive effect of 0.4 million shares of stock options outstanding included in the calculation of diluted loss per share from continuing operations or net loss per share for the six-months ended January 1, 2006, as inclusion of these shares would also be anti-dilutive.

8. **Warranties**

The Company offers warranties for certain products that it manufactures, with the warranty term generally ranging from one to two years. Warranty reserves are established for costs expected to be incurred after the sale and delivery of products under warranty, based mainly on known product failures and historical experience. Actual repair costs incurred for products under warranty are charged against the established reserve balance as incurred. Changes in the warranty reserve for the six-month periods ended December 31, 2006 and January 1, 2006 were as follows:

	Six Months Ended December 31, 2006	January 1, 2006
Balance, beginning of fiscal year	$ 430	$ 310
Additions charged to earnings for product warranties	233	300
Use of reserve for warranty obligations	(253)	(279)
Balance, end of period	$ 410	$ 331

Warranty reserves are included in accrued liabilities in the condensed consolidated balance sheets.

9. **Restructuring Costs**

As a result of the divestiture of the Company s power electronics business on October 23, 2006, the Company downsized and relocated its corporate office to Menomonee Falls, Wisconsin from Chatsworth, California. In addition, the Company was not successful in divesting its telecom power business and decided to retain and restructure the business, including relocating the manufacturing operations of the business from Dallas, Texas to Menomonee Falls.

The condensed consolidated statements of operations for the three- and six-month periods ended December 31, 2006, include severance costs of $1.9 million related to downsizing the corporate office, of which $0.6 million is included in research and development expense and $1.3 million is included in selling, general and administrative expense. Of the total

severance cost recorded in the period ended December 31, 2006, approximately $1.2 million is included in accrued liabilities in the condensed consolidated balance sheet for the period then ended and is expected to be paid in the Company s third fiscal quarter of 2007.

Costs incurred related to the restructuring and relocation of the telecom power business, including inventory charges and duplicate facility and labor costs, of $0.9 million are included in cost of sales in the condensed consolidated statements of operations for the three- and six-month periods ended December 31, 2006.

The Company expects to complete these restructuring activities during the third quarter of fiscal 2007 (March 2007), and as a result the Company s results for that period will also be impacted by restructuring costs, estimated at $0.3 million.

10. **Pension Expense**

For the three- and six-month periods ended December 31, 2006 and January 1, 2006, pension expense related to the Company s defined benefit pension plan consisted of the following:

	Three Months Ended		**Six Months Ended**	
	December 31, 2006	**January 1, 2006**	**December 31, 2006**	**January 1, 2006**
Interest Cost	$ 2,420	$ 2,440	$ 4,882	$ 4,880
Expected return on plan assets	(2,186)	(2,552)	(4,864)	(5,104)
Recognized net actuarial losses	658	1,062	1,644	2,124
Total net pension expense	$ 892	$ 950	$ 1,662	$ 1,900

Pension expense is included in selling, general and administrative expense in the accompanying condensed consolidated statements of operations.

As a result of the divestiture of the power electronics business (as discussed in Note 13 of Notes to Condensed Consolidated Financial Statements), the Company used a portion of the proceeds to make a contribution in December 2006 of $30.0 million to its defined benefit pension fund. This contribution was not contemplated in the Company s original fiscal year 2007 estimate of periodic net benefit cost. As a result of the significant contribution relative to the plan assets, the related impact on pension expense, and the divestiture of the power electronics business, the Company performed a remeasurement of its pension assets, liabilities and expense as of December 31, 2006. The remeasurement resulted in an increase of $8.6 million to the Company s pension benefit obligation and minimum pension liability due to a reduction in the discount rate from 6.38% to 5.88%, and the Company s pension expense will be $0.2 million per quarter for the remainder of fiscal 2007. The reduction in the Company s net pension benefit obligation from $45.5 million at July 2, 2006 to $25.8 million at December 31, 2006 was due to the contribution of $30.0 million recorded as a reduction in the obligation, partially offset by the remeasurement impact of $8.6 million, and pension expense of $1.7 million for the six months ended December 31, 2006, both of which were recorded as an increase in the obligation.

11. **Income Taxes**

Due to historical net losses, the Company provides valuation reserves against its U.S. deferred tax assets that result in a zero net deferred tax position (net deferred assets equal to deferred tax liabilities). A portion of the Company s deferred tax liability relates to tax-deductible amortization of goodwill that is no longer amortized for financial reporting purposes. These deferred tax liabilities are considered to have an indefinite life and are therefore ineligible to be considered as a source of future taxable income in assessing the realization of deferred tax assets.

The Company s provision for income taxes for the three- and six-months ended December 31, 2006 includes an amount of $225 and $450, respectively, to increase the Company s deferred tax liability related to tax-deductible amortization of goodwill. The remaining tax provision is comprised of income taxes of the Company s foreign subsidiary in Canada.

12. **Bank Borrowing Arrangements**

On September 30, 2005, the Company entered into an agreement with Ableco Finance LLC (Ableco) providing for an $18 million term loan and an agreement with Wells Fargo Foothill, Inc. (WFF) providing for a $13 million revolving credit facility. Borrowings under the term loan bore interest at the lender s reference rate plus 5%, or, at the Company s option, the London Interbank Offering Rate (LIBOR) plus 7.5%. Such rates could be increased by up to one percentage point depending upon the level of U.S. funded debt to EBITDA as defined in the agreement. The

term loan required quarterly principal payments of $1 million beginning in September, 2006. Borrowings under the revolving credit facility bear interest at the bank s prime lending rate plus 2.5% or, at the Company s option, LIBOR plus 4%. Borrowing levels under the revolving credit facility are determined by a borrowing base formula as defined in the agreement, based on the level of

16

eligible domestic accounts receivable and inventory. The revolving credit facility also supports the issuance of letters of credit. Borrowings under the term loan and revolving credit facility are secured by substantially all of the Company s domestic assets. The Company used the proceeds from the revolving credit facility to fully repay all outstanding obligations under its previous financing agreement with Chase Bank.

In November 2005, under terms of the financing agreements with WFF and Ableco, the Company deposited $22.6 million into an escrow account to fund the Nilssen arbitration award in the event that its appeal of the award is not successful (see Note 5 of Notes to Condensed Consolidated Financial Statements). The deposit was funded by the $18.0 million term loan and borrowings of $4.6 million from the revolving credit facility, and is reported as restricted cash in the accompanying condensed consolidated balance sheets as of December 31, 2006 and July 2, 2006.

As discussed in Notes 2 and 13 of the Notes to Condensed Consolidated Financial Statements, on October 23, 2006, the Company completed the divestiture of its power electronics business. The Company used a portion of the proceeds from the divestiture to repay all borrowings outstanding under its term loan and revolving credit facility. In accordance with provisions of the agreement with Ableco, the agreement was terminated prior to the December 2007 expiration date in exchange for a $325 prepayment penalty by the Company. The prepayment penalty is included in other expense in the consolidated statements of operations for the three- and six-month periods ended December 31, 2006. In addition, the write-off of deferred financing costs of $670 related to the term loan is included in interest expense for the three- and six-month periods ended December 31, 2006. The revolving credit facility remains in place and the Company is currently in default under certain covenants of the revolving credit agreement. The Company is in the process of obtaining a waiver and expects to modify the terms of the agreement with WFF to reflect changes in the Company s domestic asset base and expected future performance. There were no borrowings outstanding under the revolving credit facility as of December 31, 2006.

13. Divestiture of Power Electronics Business

On October 23, 2006, the Company completed the sale of its power electronics business to Power-One, Inc. (Power-One). The transaction, which satisfied all applicable regulatory approvals and other customary closing conditions, included payment by Power-One to the Company of $68.0 million in cash and the assumption by Power-One of approximately $16.0 million of the Company s debt, representing the total debt balances outstanding of the Company s subsidiary Magnetek, S.p.A. The Company used approximately $29.0 million of the proceeds to repay all its remaining outstanding debt and in December 2006 made a contribution of $30.0 million to its defined benefit pension fund. The Company intends to use the remainder of the proceeds from the sale of the business primarily to fund ongoing operations.

Pursuant to the purchase and sale agreement by and between the Company and Power-One., Power-One purchased the business through the acquisition of all of the outstanding shares of Magnetek, S.p.A., a subsidiary of the Company, and of the assets and liabilities of the U.S. division of the business. The terms of the agreement were negotiated at arms-length. The agreement provides for a final purchase price adjustment to be negotiated primarily based on changes in tangible net assets of the business from September 28, 2006 to the October 23, 2006 closing date. The agreement also provides indemnification for breaches of representations and warranties and other customary matters that the Company believes are typical for this type of transaction, including indemnifications for certain tax, legal, environmental and warranty issues.

The condensed consolidated balance sheet as of December 31, 2006 includes a total of $3.8 million in accrued liabilities, representing the Company s best estimate of remaining closing costs, the final purchase price adjustment, and contingent liabilities related to the indemnification provisions of the purchase and sale agreement. While management has used its best judgment in assessing the potential liability for these items, given the uncertainty regarding future events, it is difficult to estimate the possible timing or magnitude of any payments that may be required for liabilities subject to indemnification. The Company expects to complete negotiations regarding the final purchase price adjustment prior to the end of fiscal 2007. In the event the actual final purchase price adjustment differs from the currently recorded best estimate, the Company would record any such adjustment in the period resolved as a gain or loss on the sale of the business in discontinued operations. Similarly, any future adjustment to currently recorded closing costs estimates or contingencies related to indemnifications based upon changes in circumstances would also be recorded as a gain or loss on the sale of the business in discontinued operations.

Item 2 Management s Discussion and Analysis of Operations and Financial Condition

Overview

Magnetek is global provider of digital power control systems and we operate solely in this product category. Our systems are used primarily in material handling, motion control, telecommunications (telecom) and energy applications. We believe

that with our technical and productive resources we are well positioned to respond to increasing demand in our served markets. Our power control systems consist primarily of programmable motion control and power conditioning systems used in the following applications: cranes and hoists; elevators; wireless telecom; mining; fuel cell and wind markets. Our operations are located in North America, predominantly in Menomonee Falls, Wisconsin, the location of our Company headquarters.

During fiscal year 2005, we reclassified the assets and liabilities of our telecom power business as held for sale, and the results of operations of this business as discontinued operations. Over the past 18 months we have entered into various stages of negotiations with several interested buyers, however, we were not able to reach an agreement to sell the business. In October 2006, we decided to retain the business and initiated restructuring actions in order to improve its operating results. The accompanying financial statements reflect the reclassification of the assets and liabilities of our telecom power business as held and used, and the results of this business as continuing operations for all periods presented.

During the fourth quarter of fiscal 2006, we completed a review of various cash raising alternatives to enable us to address pending pension and debt repayment obligations, as well as provide funds for future growth initiatives, and we decided to divest our power electronics business. This business is engaged in the manufacture of embedded power electronic products, used primarily in telecom, data processing and storage, semiconductor equipment, medical instrumentation and home appliances. The business has manufacturing and administrative facilities in Italy, China, Hungary and Chatsworth, California. During the fourth quarter of fiscal year 2006, we reclassified the assets and liabilities of our power electronics business as held for sale, and the results of operations of this business as discontinued operations (see Note 2 of Notes to Condensed Consolidated Financial Statements).

In October 2006, we sold the business to Power-One, Inc. which included payment by Power-One to Magnetek of $68 million in cash and the assumption by Power-One of approximately $16 million of Magnetek s debt, subject to post closing adjustments (see Note 13 of Notes to Condensed Consolidated Financial Statements). We used a portion of the proceeds from the divestiture of the business to repay all of our outstanding bank debt, approximately $29 million, and also made a $30 million contribution to our defined benefit pension plan in December 2006.

Our results of continuing operations reflected in the accompanying consolidated financial statements include the results of power control systems (including our telecom power business) and corporate operating expenses for all periods presented. The divestiture of our power electronics business has resulted in a smaller company in terms of sales with revenue expected to exceed $100 million in our current fiscal year, but our gross margins in power control systems have historically exceeded 30%. We have also further consolidated our manufacturing operations and administrative facilities during the second quarter of fiscal 2007, relocating both our telecom manufacturing from Dallas, Texas, and our corporate office functions from Chatsworth, California, to Menomonee Falls. We believe that the resulting cost savings, together with a reduction in pension expense from the recent contribution to our pension plan and lower interest expense from reduced borrowings, should enable us to return to profitability and positive cash generation in the second half of fiscal 2007.

Continuing Operations

Demand in certain of our key markets, mainly material handling, remained strong during the second quarter of fiscal 2007 and our sales increased to $27.6 million, an increase of 6% from second quarter fiscal 2006 sales of $26.1million. Gross profit in the second quarter of fiscal 2007 was lower than the same period in fiscal 2006, due mainly to restructuring costs from the relocation of our telecom manufacturing operations and to a lesser extent sales mix in our elevator product line. Our research and development (R&D) expense increased in the second quarter of fiscal 2007 compared to the second quarter of fiscal 2006, due mainly to severance costs from downsizing and relocating our corporate office functions. We will continue to invest in R&D going forward, mainly in new product offerings for alternative energy applications and radio control for material handling, however the rate of growth in R&D spending may slow in fiscal 2007. Second quarter fiscal 2007 selling, general and administrative (SG&A) expense increased by $2.1 million compared to the second quarter of fiscal 2006, due mainly to severance and stock compensation costs related to the downsizing, relocation and reorganization of our corporate office functions and board of directors (see Notes 3 and 9 of Notes to Condensed Consolidated Financial Statements). Our second quarter fiscal 2007 results were also negatively impacted by prepayment penalties related to early debt repayment and accelerated amortization of deferred financing assets.

Our total long-term debt decreased during the second quarter of fiscal 2007 from $28.4 million at September 2006 to effectively zero at December 2006, as we used a portion of the proceeds from the divestiture of our power electronics business to repay all of our outstanding domestic bank debt, and our European debt was assumed by Power-One upon the purchase of the business. We contributed $30 million to our defined benefit pension plan in fiscal 2007, and under current funding regulations, no contributions are expected until April 2008. Future required contributions will depend on future interest rate levels, values in equity and fixed income markets, and the level and timing of interim contributions we may make to the plan, and could still be significant. Pension expense recorded for financial reporting purposes is also dependent

upon these factors, but is expected to be substantially lower in future periods as compared to recent historical recorded expense due primarily to the impact of the recent contribution on pension expense calculated under accounting rules.

We intend to focus our development and marketing capabilities on internal sales growth opportunities across all product lines, with a near-term emphasis on wind and elevator products, and intend to complete our telecom relocation in our third fiscal quarter (ending March 2007) and focus on improving our manufacturing flow and related efficiency in that business to improve our margins. We also plan to complete the consolidation of our administrative operations during the third quarter of fiscal 2007, and will continue to review further administrative cost reduction actions. However future sustained profitability is dependent upon increasing sales revenue, improvement in gross margins, successful implementation of our strategy to penetrate higher margin markets, and successful introduction of new product offerings.

Discontinued Operations

The results of our power electronics business, as well as certain expenses related to previously divested businesses, have been classified as discontinued operations in the accompanying condensed consolidated financial statements and footnotes for all periods presented. The assets and liabilities of our power electronics business are classified as held for sale in the accompanying condensed consolidated balance sheet as of July 1, 2006.

Our second quarter fiscal 2007 loss from discontinued operations was $1.6 million, due mainly to losses incurred in our power electronics business of $1.3 million prior to its divestiture in October 2006. The loss from discontinued operations for the periods ended December 31, 2006 does not include any gain or loss on the divestiture of the power electronics business (see Note 13 of Notes to Condensed Consolidated Financial Statements). Costs associated with other previously owned business were $0.3 million in the period. These costs have historically included charges for an arbitration award in a patent infringement claim and related legal fees (see Note 5 of Notes to Consolidated Financial Statements), as well as certain expenses for product liability claims, environmental issues, and asbestos claims. All of these issues relate to businesses we no longer own and most relate to indemnification agreements we provided when we divested those businesses.

Going forward, our discontinued operations will include additional costs we may incur related to businesses no longer owned and may include additional costs above those currently estimated and accrued related to the divestiture of our power electronics business.

Critical Accounting Policies

The following discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements. In preparing financial statements in conformity with accounting principles generally accepted in the United States, we must make estimates and assumptions that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Such estimates are based upon historical experience and other assumptions believed to be reasonable given known circumstances. Actual results could differ from those estimates. On an ongoing basis, we evaluate and update our estimates, including those related to accounting for inventories, goodwill, pension benefits and reserves for litigation and environmental issues. We consider the following policies critical to understanding our financial position and results of operations.

Accounts Receivable

Accounts receivable represent amounts due from customers in the ordinary course of business. We are subject to losses from uncollectible receivables in excess of our allowances. We maintain allowances for doubtful accounts for estimated losses from customers inability to make required payments. In order to estimate the appropriate level of this allowance, we analyze historical bad debts, customer concentrations, current customer creditworthiness, current economic trends and changes in customer payment patterns. Our total allowance includes a specific allowance based on identification of customers where we feel full payment is in doubt, as well as a general allowance calculated based on our historical losses on accounts receivable as a percentage of historical sales. We believe that our methodology has been effective in accurately quantifying our allowance for doubtful accounts and do not anticipate changing our methodology in the future. However, if the financial conditions of any of our customers were to deteriorate and impair their ability to make payments, additional allowances may be required in future periods. We believe that all appropriate allowances have been provided.

Inventories

Our inventories are stated at the lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method, including material, labor and factory overhead. We identify potentially obsolete and excess inventory by evaluating overall inventory levels in relation to expected future requirements and market conditions, and provisions for excess and obsolete

inventory and inventory valuation are recorded accordingly. Items with no usage for the past twelve months and no expected future usage are considered obsolete, and are disposed of or fully reserved. Reserves for excess inventory are determined based upon historical and anticipated usage as compared to quantities on hand. Excess inventory is defined as inventory items with on-hand quantities in excess of one year s usage and specified percentages are applied to the excess inventory value in determining the reserve. Our assumptions have not changed significantly in the past, and we believe they are not likely to change in the foreseeable future. We feel that our assumptions regarding inventory valuation have been accurate in the past.

Long-Lived Assets and Goodwill

We periodically evaluate the recoverability of our long-lived assets, including property, plant and equipment. Impairment charges are recorded in operating results when the undiscounted future expected cash flows derived from an asset are less than the carrying value of the asset. We are required to perform annual impairment tests of our goodwill, and may be required to test more frequently in certain circumstances. We have elected to perform our annual impairment test in the fourth quarter of our fiscal year. Our power controls systems business is our only reporting unit under SFAS No. 142.

In assessing potential impairment, we make significant estimates and assumptions regarding the discounted future cash flows of our reporting units to determine the fair value of those reporting units. Such estimates include, but are not limited to, projected future operating results, working capital ratios, cash flow, terminal values, market discount rates and tax rates. We review the accuracy of our projections by comparing them to our actual results annually, and have determined that, historically, our cash flow estimates used in determining the fair value of our reporting units have been reasonably accurate. We use the results of this analysis as well as projected operating results to modify our estimates annually. However, if circumstances cause these estimates to change in the future, or if actual circumstances vary significantly from these assumptions, this could result in additional goodwill impairment charges. We cannot predict the occurrence of future events that may adversely affect our reported goodwill balance.

Pension Benefits

We sponsor a defined benefit plan that covers a number of current and former employees in the U.S. The valuation of our pension plan requires the use of assumptions and estimates that attempt to anticipate future events to develop actuarial valuations of expenses, assets and liabilities. These assumptions include discount rates, expected rates of return on plan assets and mortality rates. We consider market conditions, including changes in investment returns and interest rates, in making these assumptions. Our plan assets are comprised mainly of common stock and bond funds. The expected rate of return on plan assets is a long-term assumption and is generally not changed on an annual basis. The discount rate reflects the market for high-quality fixed income debt instruments and is subject to change each year. Changes in assumptions typically result in actuarial gains or losses that are amortized in accordance with the methods specified in FAS Statement No. 87. Significant differences between our assumptions and actual future investment return or discount rates could have a material impact on our financial position or results of operations and related funding requirements.

Following the divestiture of our power electronics business, we contributed $30 million to our defined benefit pension fund in December 2006. The contribution was not contemplated in our original fiscal 2007 estimate of periodic net benefit cost. As a result of the significant contribution and the related impact on pension expense, as well as the divestiture of our power electronics business, we performed a remeasurement of pension assets, liabilities and periodic net benefit cost as of December 31, 2006. Our pension benefit obligation and minimum pension liability were increased by $8.6 million, due mainly to a reduction in our discount rate assumption to 5.9% from a rate of 6.4% in the original estimate for fiscal 2007 prepared in June 2006. Our pension expense will be reduced to $0.2 million per quarter for the remainder of fiscal 2007 beginning in our third fiscal quarter.

Reserves for Contingencies

We periodically record the estimated impacts of various conditions, situations or circumstances involving uncertain outcomes. The accounting for such events is prescribed under SFAS No. 5, *Accounting for Contingencies*. SFAS No. 5 defines a contingency as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur.

SFAS No. 5 does not permit the accrual of gain contingencies under any circumstances. For loss contingencies, the loss must be accrued if (1) information is available that indicates it is probable that the loss has been incurred, given the likelihood of uncertain events; and (2) that the amount of the loss can be reasonably estimated.

The accrual of a contingency involves considerable judgment on our part. We use our internal expertise, and outside experts as necessary, to help estimate the probability that a loss has been incurred and the amount or range of the loss.

20

Income Taxes

We operate in several taxing jurisdictions and are subject to a variety of income and related taxes. Judgment is required in determining our provision for income taxes and related tax assets and liabilities. We believe we have reasonably estimated our tax positions for all jurisdictions for all open tax periods. It is possible that, upon closure of our tax periods, our final tax liabilities could differ from our estimates.

We record deferred income tax assets in tax jurisdictions where we generate losses for income tax purposes. We also record valuation allowances against these deferred tax assets in accordance with SFAS No. 109, *Accounting for Income Taxes*, when, in our judgment, the deferred income tax assets will likely not be realized in the foreseeable future.

Results of Operations - Three Months Ended December 31, 2006 and January 1, 2006

Net Sales and Gross Profit

Net sales for the three months ended December 31, 2006 were $27.6 million, an increase of 5.7% from the three months ended January 1, 2006 sales of $26.1 million. The increase was mainly due to higher sales of material handling products of $1.0 million. Net sales by product line were as follows, in millions:

	Three Months Ended							
	December 31, 2006				**January 1, 2006**			
Material handling	$	15.9	58	%	$	14.9	57	%
Elevator motion control	5.1		18	%	4.5		17	%
Telecom power systems	4.9		18	%	4.3		17	%
Energy systems	1.7		6	%	2.4		9	%
Total net sales	$	27.6	100	%	$	26.1	100	%

Gross profit for the three months ended December 31, 2006 was $7.1 million, or 25.6% of sales, versus $7.9 million, or 30.4% of sales, in the three months ended January 1, 2006. The reduction in gross profit as a percentage of sales in the three months ended December 31, 2006 as compared to the three months ended January 1, 2006 was due to restructuring costs of $0.9 million related to the relocation of our telecom manufacturing operations, unfavorable sales mix within our elevator product line, and lower sales in our energy systems business due to the divestiture of our residential solar power inverter product line.

Research and Development, Selling, General and Administrative

R&D expense was $1.6 million, or 5.8% of sales, in the three months ended December 31, 2006, compared to the R&D expense of $1.3 million, or 5.0% of sales, for the three months ended January 1, 2006. R&D expense in the three months ended December 31, 2006 includes $0.6 million in severance related to restructuring of our corporate office functions. We continue to invest in product development for new markets and applications such as alternative energy products for wind applications.

SG&A expense was $9.2 million (33.3% of sales) in the three months ended December 31, 2006 versus $7.1 million (27.3% of sales) in the three months ended January 1, 2006. Selling expenses in the three months ended December 31, 2006 were $2.7 million, comparable to $2.6 million in the three months ended January 1, 2006, due to higher volume related commissions. General and administrative (G&A) expense was $6.5 million in the three months ended December 31, 2006 compared to $4.5 million in the three months ended January 1, 2006, due to higher stock-based compensation expense of $1.1 million (see Note 3 of Notes to Condensed Consolidated Financial Statements) and $1.3 million in severance costs in the three months ended December 31, 2006 (see Note 9 of Notes to Condensed Consolidated Financial Statements).

Loss from Operations

Our loss from operations for the three months ended December 31, 2006 was $3.7 million compared to a loss from operations of $0.5 million for the three months ended January 1, 2006. The increase in loss from operations in the three months ended December 31, 2006 as compared to the three months ended January 1, 2006 was mainly due to restructuring and relocation costs of $3.9 million included in our loss from operations for the three months ended December 31, 2006.

Interest Income and Expense and Other Expense

Interest income was $0.9 million and interest expense was $1.1 million in the three months ended December 31, 2006. Interest income was $0.1 million and interest expense was $0.8 million in the three months ended January 1, 2006. The increase in interest income in the three months ended December 31, 2006 was due to higher cash balances held in short-term investments and $0.3 million in interest income related to a previous tax settlement.

The increase in interest expense in the three-month period ended December 31, 2006 was mainly due to the write-off of deferred financing assets of $0.7 million from the early retirement of debt. Interest expense in the three months ended January 1, 2006 reflects outstanding borrowings associated with a patent arbitration award (see Note 5 of Notes to Condensed Consolidated Financial Statements). In November 2005, we deposited $22.6 million into escrow to satisfy payment of the award in the event our appeal is not successful. The deposit was funded mainly by an $18.0 million term loan, which bore interest at rates of 11% while we received interest on the escrow deposit at a rate of 4%. The term loan was repaid in October 2006, and as a result, our other expense of $0.3 million in the three months ended December 31, 2006 is comprised entirely of a prepayment penalty related to the early repayment of that debt.

Provision for Income Taxes

Despite the pretax loss of $4.2 million in the three months ended December 31, 2006 and the pretax loss of $1.2 million in the three months ended January 1, 2006, we recorded tax provisions in those periods of $0.4 million and $0.3 million respectively, due to non-cash tax provisions related to goodwill amortization and to a lesser extent, provisions for income taxes on our pretax income in Canada (see Note 11 of Notes to Condensed Consolidated Financial Statements).

Loss from Continuing Operations

We recorded a loss from continuing operations of $4.6 million in the three months ended December 31, 2006, or $0.16 loss per share on both a basic and diluted basis, compared to a loss from continuing operations of $1.6 million in the three months ended January 1, 2006, or $0.05 loss per share on both a basic and diluted basis.

Loss from Discontinued Operations

Our loss from discontinued operations for the three months ended December 31, 2006 was $1.6 million, or $0.06 loss per share on both a basic and diluted basis, compared to a loss from discontinued operations of $0.2 million, or $0.01 loss per share on both a basic and diluted basis, for the three months ended January 1, 2006. Loss from discontinued operations in the three months ended December 31, 2006 was comprised mainly of losses in our discontinued power electronics business of $1.3 million and expenses related to previously divested businesses of $0.3 million, mainly legal fees and other costs associated with the patent infringement claim and asbestos claims. Loss from discontinued operations of $0.2 million in the three months ended January 1, 2006 was comprised of net income from our discontinued power electronics business of $0.7 million, partially offset by expenses related to previously divested businesses of $0.9 million, mainly legal fees and other costs associated with the patent infringement claim.

Net Loss

Our net loss was $6.2 million in the three months ended December 31, 2006, or $0.21 loss per share, basic and diluted, compared to a net loss of $1.7 million in the three months ended January 1, 2006, or $0.06 loss per share on both a basic and diluted basis.

Results of Operations - Six Months Ended December 31, 2006 and January 1, 2006

Net Sales and Gross Profit

Net sales for the six months ended December 31, 2006 were $53.5 million, an increase of 7.8% from the six months ended January 1, 2006 sales of $49.7 million. The increase was mainly due to higher sales of material handling products of $1.9 million and higher sales of elevator products of $1.7 million. Net sales by product line were as follows, in millions:

	Six Months Ended December 31, 2006			January 1, 2006		
Material handling	$ 31.4	59	%	$ 29.5	59	%
Elevator motion control	10.0	19	%	8.3	17	%
Telecom power systems	8.3	16	%	7.8	16	%
Energy systems	3.8	7	%	4.1	8	%
Total net sales	$ 53.5	100	%	$ 49.7	100	%

Gross profit for the six months ended December 31, 2006 was $14.5 million, or 27.0% of sales, versus $15.2 million, or 30.6% of sales, in the six months ended January 1, 2006. The reduction in gross profit as a percentage of sales in the six months ended December 31, 2006 as compared to the six months ended January 1, 2006 was due to unfavorable sales mix of $1.0 million and restructuring costs of $0.9 million related to the relocation of our telecom manufacturing operations, partially offset by increased margin on higher sales of $1.1 million.

Research and Development, Selling, General and Administrative

R&D expense was $2.8 million, or 5.2% of sales, in the six months ended December 31, 2006, compared to the R&D expense of $2.5 million, or 5.0% of sales, for the six months ended January 1, 2006. R&D expense in the six months ended December 31, 2006 includes $0.6 million in severance related to restructuring of our corporate office functions. We continue to invest in product development for new markets and applications such as alternative energy products for wind applications and expect our R&D expense to approximate $1.0 to $1.2 million per quarter for the remainder of the fiscal year.

SG&A expense was $16.6 million (31.0% of sales) in the six months ended December 31, 2006 versus $13.7 million (27.7% of sales) in the six months ended January 1, 2006. Selling expenses in the six months ended December 31, 2006 were $5.4 million, an increase of $0.5 million compared to $4.9 million in the six months ended January 1, 2006, due to higher volume related commissions. G&A expense was $11.2 million in the six months ended December 31, 2006 compared to $8.8 million in the six months ended January 1, 2006, due to higher stock-based compensation expense of $1.1 million (see Note 3 of Notes to Condensed Consolidated Financial Statements) and $1.3 million in severance costs in the six months ended December 31, 2006 (see Note 9 of Notes to Condensed Consolidated Financial Statements).

Loss from Operations

Our loss from operations for the six months ended December 31, 2006 was $4.9 million compared to a loss from operations of $1.0 million for the six months ended January 1, 2006. The increase in loss from operations in the six months ended December 31, 2006 as compared to the six months ended January 1, 2006 was mainly due to restructuring and relocation costs of $3.9 million included in our loss from operations for the six months ended December 31, 2006.

Interest Income and Expense and Other Expense

Interest income was $1.2 million and interest expense was $2.1 million in the six months ended December 31, 2006. Interest income was $0.1 million and interest expense was $1.3 million in the six months ended January 1, 2006. The increase in interest income in the six months ended December 31, 2006 was due to higher cash balances held in short-term investments during November and December 2006 and $0.3 million in interest income related to a previous tax settlement.

The increase in interest expense in the six-month period ended December 31, 2006 was mainly due to the write-off of deferred financing assets of $0.7 million from the early retirement of debt. Interest expense in the six months ended January 1, 2006 reflects outstanding borrowings associated with a patent arbitration award (see Note 5 of Notes to Condensed Consolidated Financial Statements). In November 2005, we deposited $22.6 million into escrow to satisfy payment of the award in the event our appeal is not successful. The deposit was funded mainly by an $18.0 million term loan, which bore interest at rates of 11% while we received interest on the escrow deposit at a rate of 4%. The term loan was repaid in October 2006, and as a result, our other expense of $0.3 million in the six months ended December 31, 2006 is comprised entirely of a prepayment penalty related to the early repayment of that debt.

Provision for Income Taxes

Despite the pretax loss of $6.2 million in the six months ended December 31, 2006 and the pretax loss of $2.1 million in the six months ended January 1, 2006, we recorded tax provisions in those periods of $0.6 million and $0.7 million respectively, due to non-cash tax provisions related to goodwill amortization and to a lesser extent, provisions for income taxes on our pretax income in Canada (see Note 11 of Notes to Condensed Consolidated Financial Statements).

Loss from Continuing Operations

We recorded a loss from continuing operations of $6.8 million in the six months ended December 31, 2006, or $0.23 loss per share on both a basic and diluted basis, compared to a loss from continuing operations of $2.8 million in the six months ended January 1, 2006, or $0.10 loss per share on both a basic and diluted basis.

Income (Loss) from Discontinued Operations

Our loss from discontinued operations for the six months ended December 31, 2006 was $2.6 million, or $0.09 loss per share on both a basic and diluted basis, compared to a slight income from discontinued operations, or $0.00 income per share on both a basic and diluted basis, for the six months ended January 1, 2006. Loss from discontinued operations in the six months ended December 31, 2006 was comprised mainly of losses in our discontinued power electronics business of $2.3 million and expenses related to previously divested businesses of $0.3 million, mainly legal fees and other costs associated with the patent infringement claim and asbestos claims. Income from discontinued operations in the six months ended January 1, 2006 was comprised of net income from our discontinued power electronics business of $1.4 million, partially offset by expenses related to previously divested businesses of $1.3 million, mainly legal fees and other costs associated with the patent infringement claim.

Net Loss

Our net loss was $9.4 million in the six months ended December 31, 2006, or $0.32 loss per share, basic and diluted, compared to a net loss of $2.8 million in the six months ended January 1, 2006, or $0.10 loss per share on both a basic and diluted basis.

Liquidity and Capital Resources

Our cash balance, excluding restricted cash, increased $7.2 million during the six months ended December 31, 2006, from $0.1 million at July 2, 2006 to $7.3 million at December 31, 2006. During the six months ended December 31, 2006, our accounts receivable balances increased $2.8 million, while accounts payable increased $2.0 million and inventories decreased $0.5 million. Our capital expenditures in the six months ended December 31, 2006 were less than $0.3 million; however we currently plan to add capacity for the production of wind inverters. Including expenditures for this capacity, we do not anticipate capital expenditures in fiscal 2007 will exceed $2.0 million. The expected amount of capital expenditures could change depending upon changes in revenue levels, our financial condition and the general economy.

As discussed in Notes 2 and 13 of the Notes to Condensed Consolidated Financial Statements, on October 23, 2006, we sold our power electronics business to Power-One for $68.0 million in cash and the assumption of approximately $16.0 million in outstanding debt in Europe. We used approximately $29.0 million of the proceeds from the divestiture to repay all borrowings outstanding under our term loan with Ableco and revolving credit facility with WFF in October 2006. Pursuant to the terms of the loan agreement with Ableco, the agreement was terminated prior to the December 2007 expiration date in exchange for our payment to Ableco of $325. The revolving credit facility remains in place and we are currently in default under certain covenants of the revolving credit agreement. We are in the process of obtaining a waiver and expect to modify the terms of the agreement with WFF to reflect changes in our domestic asset base and expected future performance. There were no borrowings outstanding under the revolving credit facility as of December 31, 2006.

Primarily as a result of the decline in interest rates over the past several years, the accumulated benefit obligation of our defined benefit pension plan currently exceeds plan assets. We used a portion of the proceeds from the divestiture of our power electronics business to contribute $30.0 million to our pension fund in December 2006 and under current funding regulations, actuarial projections indicate no contributions to the plan would be required before April 2008. Future required contributions will depend on future interest rate levels, values in equity and fixed income markets, and the level and timing of interim contributions we may make to the plan, and could still be significant.

We are subject to certain potential environmental and legal liabilities associated primarily with past divestitures (see Note 5 of Notes to Condensed Consolidated Financial Statements). In the fourth quarter of

24

fiscal 2005, a decision was rendered in a patent infringement action brought against us by Ole K. Nilssen. In settlement of pending litigation, we agreed to submit the matter to binding arbitration, and in May 2005, the arbitrator awarded damages to Mr. Nilssen of $23.4 million, to be paid within ten days of the award. Nilssen s counsel filed a motion to enter the award in U.S. District Court for the Northern District of Illinois, and we filed a counter-motion to vacate the award on grounds that it was fraudulently obtained. Our request for oral argument was granted and the hearing was held on October 19, 2005. The judge is expected to render his decision by mail after further consideration. An unfavorable decision by the Court could result in payment of the award of $22.6 million, net of previously paid amounts, to Nilssen, which would have a material adverse effect on our cash flows during the period in which payment would be made. We have adequate resources to support payment of the award if such a payment is necessary, as we currently have $22.6 million cash in an interest-earning escrow account.

We did not have any off-balance sheet arrangements or variable interest entities as of December 31, 2006.

Based upon current plans and business conditions, we believe that current cash balances, borrowing capacity under our revolving credit facility and internally generated cash flows will be sufficient to fund anticipated operational needs, capital expenditures and other commitments over the next 12 months.

Caution Regarding Forward-Looking Statements and Risk Factors

This document, including documents incorporated herein by reference, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words believe , expect , estimate , anticipate , intend , may , might , will , would , cou predict , or similar words and phrases generally identify forward-looking statements. Forward-looking statements are inherently subject to risks and uncertainties which in many cases are beyond our control and which cannot be predicted or quantified. As a result, future events and actual results could differ materially from those set forth in, contemplated by, or underlying forward-looking statements. Forward-looking statements contained in this document speak only as of the date of this document or, in the case of any document incorporated by reference from another document, the date of that document. We do not have any obligation to publicly update or revise any forward-looking statement contained or incorporated by reference in these documents to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time.

Our future results of operations and the other forward-looking statements contained in this filing, including this section titled Management s Discussion and Analysis of Financial Condition and Results of Operations , involve a number of risks and uncertainties. In particular, the statements regarding future economic conditions, our goals and strategies, new product introductions, penetration of new markets, projections of sales revenues, manufacturing costs and operating costs, pricing of our products and raw materials required to manufacture our products, gross margin expectations, relocation and outsourcing of production capacity, capital spending, research and development expenses, the outcome of pending legal proceedings and environmental matters, tax rates, sufficiency of funds to meet our needs including contributions to our defined benefit pension plan, and our plans for future operations, as well as our assumptions relating to the foregoing, are all subject to risks and uncertainties.

A number of factors could cause our actual results to differ materially from our expectations. We are subject to all of the business risks facing public companies, including business cycles and trends in the general economy, financial market conditions, changes in interest rates, demand variations and volatility, potential loss of key personnel, supply chain disruptions, government legislation and regulation, and natural causes. Additional risks and uncertainties include but are not limited to industry conditions, competitive factors such as technology and pricing pressures, business conditions in our served markets, dependence on significant customers, increased material costs, risks and costs associated with acquisitions and divestitures, environmental matters and the risk that our ultimate costs of doing business exceed present estimates. This list of risk factors is not all-inclusive, as other factors and unanticipated events could adversely affect our financial position or results of operations. Further information on factors that could affect our financial results can be found in our Form 10-K filing with the Securities and Exchange Commission for the year ended July 2, 2006, under the heading Risk Factors Affecting the Company s Outlook .

Item 3 Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risks in the areas of foreign exchange and interest rates. To mitigate the effect of such risks, from time to time we selectively use specific financial instruments. Hedging transactions can be entered into under Company policies and procedures and are monitored monthly. Company policy prohibits the use of such financial instruments for

trading or speculative purposes. There have been no material changes in the market risks that we reported in our Annual Report on Form 10-K dated July 2, 2006. A discussion of our accounting policies for derivative financial instruments is included in the Summary of Significant Accounting Policies under Note 1 in the Notes to Condensed Consolidated Financial Statements. Our continuing operations did not have any outstanding hedge instruments or contracts at December 31, 2006, and July 2, 2006.

Interest Rates

The fair value of our debt was effectively zero at December 31, 2006. Our debt balance of $37 was comprised entirely of capital lease obligations. As a result, at December 31, 2006, a hypothetical 10% adverse change in interest rates would have a negligible impact on our annual interest expense, as we have fully repaid all of our debt outstanding under our term loan and revolving credit facility with proceeds from the divestiture of our power electronics business (see Liquidity and Capital Resources and Note 12 of Notes to Condensed Consolidated Financial Statements).

Foreign Currency Exchange Rates

We generally do not enter into foreign exchange contracts to protect against reductions in value and volatility of future cash flows caused by changes in exchange rates, but we may selectively enter into foreign exchange contracts to hedge certain exposures. Gains and losses on these non-U.S.-currency investments would generally be offset by corresponding losses and gains on the related hedging instruments, resulting in negligible net exposure.

We had no foreign currency contracts outstanding at December 31, 2006 and July 2, 2006.

Item 4 Controls and Procedures

In connection with this Form 10-Q, under the direction of our Chief Executive Officer and Chief Financial Officer, we evaluated our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, and internal control over financial reporting and concluded that (i) our disclosure controls and procedures were effective as of December 31, 2006, and (ii) no change in internal control over financial reporting occurred during the quarter ended December 31, 2006, that has materially affected, or is reasonably likely to materially affect, such internal control over financial reporting.

Attached as exhibits to this Form 10-Q are certifications of the Company s Chief Executive Officer and Chief Financial Officer, which are required in accordance with Rule 13a-14 of the Securities Exchange Act of 1934. This Controls and Procedures section includes information concerning the controls and evaluation thereof referred to in the attached certifications, and it should be read in conjunction with the attached certifications for a more complete understanding of the topics presented.

PART II - OTHER INFORMATION

Item 1 Legal Proceedings

In April 1998, Ole K. Nilssen (Nilssen) filed a lawsuit in the U.S. District Court for the Northern District of Illinois alleging infringement by the Company of seven of his patents pertaining to electronic ballast technology, and seeking unspecified damages and injunctive relief to preclude the Company from making, using or selling products allegedly infringing his patents. The Company denied that its products infringed any valid patent and filed a response asserting affirmative defenses, as well as a counterclaim for a judicial declaration that its products do not infringe the patents asserted by Mr. Nilssen and also that the asserted patents are invalid. In June 2001, the Company sold its lighting business to Universal Lighting Technologies, Inc. (ULT), and agreed to provide a limited indemnification against certain claims of infringement that Nilssen might allege against ULT. In April 2003, Nilssen s lawsuit and the counterclaims were dismissed with prejudice and both parties agreed to submit limited issues in dispute to binding arbitration before an arbitrator with a relevant technical background. The arbitration occurred in November, 2004 and a decision awarding Nilssen $23.4 million was issued on May 3, 2005, to be paid within ten days of the award. Nilssen s counsel filed a motion to enter the award in U.S. District Court for the Northern District of Illinois, and Magnetek filed a counter-motion to vacate the award for a number of reasons, including that the award was fraudulently obtained. Magnetek s request for oral argument was granted and the hearing took place on October 19, 2005. A decision has not been announced. An unfavorable decision by the Court would likely result in payment of the award to Nilssen.

In February 2003, Nilssen filed a second lawsuit in the U.S. District Court for the Northern District of Illinois alleging infringement by ULT of twenty-nine of his patents pertaining to electronic ballast technology, and seeking unspecified damages and injunctive relief to preclude ULT from making, using or selling products allegedly infringing his patents. ULT made a claim for indemnification, which the Company accepted, subject to the limitations set forth in the sale agreement.

26

The case is now pending in the Central District of Tennessee. Nilssen voluntarily dismissed all but four of the patents from the lawsuit. The Company denies that the products for which it has an indemnification obligation to ULT infringe any valid patent and responded on behalf of ULT asserting affirmative defenses, as well as a counterclaim for a judicial declaration that the patents are unenforceable and invalid and that the products do not infringe Nilssen s patents. ULT requested a re-examination of the patents at issue by the Patent and Trademark Office and the request was granted. Meanwhile, the case against ULT has been stayed pending Nilssen s appeal of an unfavorable decision against him in another case that could influence the outcome of his lawsuits against ULT. The Company will continue to aggressively defend the claims against ULT that are subject to defense and indemnification; however, an unfavorable decision could have a material adverse effect on the Company s financial position, cash flows and results of operations.

Effect of Fruit of the Loom Bankruptcy (Bridgeport, Connecticut)

In 1986, the Company acquired the stock of Universal Manufacturing Company (Universal) from a predecessor of Fruit of the Loom (FOL), and the predecessor agreed to indemnify the Company against certain environmental liabilities arising from pre-acquisition activities at a facility in Bridgeport, Connecticut. Environmental liabilities covered by the indemnification agreement include completion of additional cleanup activities, if any, at the Bridgeport facility (sold in connection with the sale of the transformer business in June 2001) and defense and indemnification against liability for potential response costs related to offsite disposal locations. FOL, the successor to Universal s indemnification obligation, filed a petition for Reorganization under Chapter 11 of the Bankruptcy Code in 1999 and the Company filed a proof of claim in the proceeding for obligations related to the environmental indemnification agreement. The Company believes that FOL had substantially completed the clean-up obligations required by the indemnification agreement prior to the bankruptcy filing. In November 2001, the Company and FOL entered into an agreement involving the allocation of certain potential tax benefits and Magnetek withdrew its claims in the bankruptcy proceeding. FOL s obligation to the state of Connecticut was not discharged in the reorganization proceeding. In October 2006, the owner of the Bridgeport facility filed a lawsuit in Superior Court, J.D. of Fairfield, Connecticut alleging that the Company is obligated to remediate environmental contamination at the facility. The Company has filed a Motion to Stay and Remand the matter to the Connecticut Department of Environmental Protection (DEP) on the basis that DEP has primary jurisdiction to determine the need and responsibility for any further remediation. FOL s inability to satisfy its remaining obligations related to the Bridgeport facility and any offsite disposal locations, or an unfavorable ruling in the lawsuit with the owner of the Bridgeport facility, or the discovery of additional environmental contamination at the Bridgeport facility could have a material adverse effect on the Company s financial position, cash flows or results of operations.

Item 1A Risk Factors

There have been no material changes to the risk factors disclosed in our Annual Report on Form 10-K for the year ended July 2, 2006.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds

There were no unregistered sales of equity securities and there were no repurchases of equity securities during our second fiscal quarter ended December 31, 2006.

Item 3 Defaults upon Senior Securities

None.

Item 4 Submission of Matters to a Vote of Security Holders

None.

Item 5 Other Information

None.

Item 6 Exhibits

(a) Index to Exhibits

31.1 Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934. *

31.2 Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934. *

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. *

---

* Filed with this Report on Form 10-Q.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MAGNETEK, INC.
(Registrant)

Date: February 9, 2007

/s/ David P. Reiland
David P. Reiland
President and Chief Executive Officer
(Duly authorized officer of the Registrant
and principal executive officer)

Date: February 9, 2007

/s/ Marty J. Schwenner
Marty J. Schwenner
Vice-President and Chief Financial Officer
(Duly authorized officer of the Registrant
and principal financial officer)

---

s new roman">29,587 $— $218,720

Income from operations	47,875	2,484	(13,173)	37,186
Depreciation and amortization expense	3,995	1,106	233	5,334
Net capital expenditures	1,533	23	173	1,729
Nine months ended October 1, 2011				
Net sales	$521,137	$91,010	$—	$612,147
Income from operations	127,118	13,706	(37,026)	103,798
Depreciation and amortization expense	11,886	2,207	574	14,667
Net capital expenditures	4,327	162	391	4.880
Total assets	827,276	139,618	63,473	1,030,367
Long-lived assets	602,164	85,263	33,760	721,187
Three months ended October 2, 2010				

Net sales	$156,081	$21,712	$—	$177,793
Income from operations	38,002	4,040	(10,031)	32,011
Depreciation and amortization expense	3,257	438	154	3,849
Net capital expenditures	400	65	138	603
Nine months ended October 2, 2010				
Net sales	$450,036	$61,852	$—	$511,888
Income from operations	107,042	12,076	(30,943)	88,175
Depreciation and amortization expense	10,040	1,150	466	11,656
Net capital expenditures	2,492	167	349	3,008
Total assets	709,733	104,377	52,528	866,638
Long-lived assets	524,905	58,271	30,169	613,345

(1)Non-operating expenses are not allocated to the operating segments. Non-operating expenses consist of interest expense and deferred financing amortization, foreign exchange gains and losses and other income and expense items outside of income from operations.

(2) Includes corporate and other general company assets and operations.

Long-lived assets by major geographic region are as follows (in thousands):

	Oct 1, 2011	Oct 2, 2010
United States and Canada	$ 583,632	$ 586,151
Asia	34,254	1,826
Europe and Middle East	102,274	24,412
Latin America	1,027	956
Total international	$ 137,555	$ 27,194
	$ 721,187	$ 613,345

Net sales by major geographic region were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	Oct 1, 2011	Oct 2, 2010	Oct 1, 2011	Oct 2, 2010
United States and Canada	$ 149,891	$ 141,179	$ 446,071	$ 410,444
Asia	17,228	12,503	41,052	29,724
Europe and Middle East	41,628	17,675	95,248	56,915
Latin America	9,973	6,436	29,776	14,805
Total international	$ 68,829	$ 36,614	$ 166,076	$ 101,444
	$ 218,720	$ 177,793	$ 612,147	$ 511,888

13) Employee Retirement Plans

(a) Pension Plans

The company maintains a non-contributory defined benefit plan for its employees at the Smithville, Tennessee facility, which was acquired as part of the New Star International Holdings, Inc. ("Star") acquisition. Benefits are determined based upon retirement age and years of service with the company. This defined benefit plan was frozen on April 1, 2008 and no further benefits accrue to the participants beyond this date. Plan participants will receive or continue to receive payments for benefits earned on or prior to April 1, 2008 upon reaching retirement age.

The company maintains a non-contributory defined benefit plan for its union employees at the Elgin, Illinois facility. Benefits are determined based upon retirement age and years of service with the company. This defined benefit plan was frozen on April 30, 2002 and no further benefits accrue to the participants beyond this date. Plan participants will receive or continue to receive payments for benefits earned on or prior to April 30, 2002 upon reaching retirement age. The employees participating in the defined benefit plan were enrolled in a newly established 401K savings plan on July 1, 2002, further described below.

The company also maintains a retirement benefit agreement with its Chairman. The retirement benefits are based upon a percentage of the Chairman's final base salary. Additionally, the company maintains a retirement plan for non-employee directors who served on the Board of Directors prior to 2004. In November 2010, the Board of Directors approved a revision to the directors' compensation program that resulted in the plan being frozen and the benefits being distributed to the plan participants. Benefit distributions were made in December 2010 and January 2011. As of October 1, 2011, there were no longer any participants in the plan for non-employee directors. This plan is not available to any new non-employee directors.

(b) 401K Savings Plans

The company maintains two separate defined contribution 401K savings plans covering all employees in the United States. These two plans separately cover the union employees at the Elgin, Illinois facility and all other remaining union and non-union employees in the United States. The company makes profit sharing contributions to the various plans in accordance with the requirements of the plan. Profit sharing contributions for the Elgin Union 401K savings plans are made in accordance with the agreement.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Informational Notes

This report contains forward-looking statements subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995. The company cautions readers that these projections are based upon future results or events and are highly dependent upon a variety of important factors which could cause such results or events to differ materially from any forward-looking statements which may be deemed to have been made in this report, or which are otherwise made by or on behalf of the company. Such factors include, but are not limited to, volatility in earnings resulting from goodwill impairment losses which may occur irregularly and in varying amounts; variability in financing costs; quarterly variations in operating results; dependence on key customers; international exposure; foreign exchange and political risks affecting international sales; ability to protect trademarks, copyrights and other intellectual property; changing market conditions; the impact of competitive products and pricing; the timely development and market acceptance of the company's products; the availability and cost of raw materials; and other risks detailed herein and from time-to-time in the company's Securities and Exchange Commission ("SEC") filings, including the company's 2010 Annual Report on Form 10-K.

Net Sales Summary
(dollars in thousands)

	Three Months Ended				Nine Months Ended			
	Oct 1, 2011		Oct 2, 2010		Oct 1, 2011		Oct 2, 2010	
	Sales	Percent	Sales	Percent	Sales	Percent	Sales	Percent
Business Divisions:								
Commercial Foodservice	$189,133	86.5	$156,081	87.8	$521,137	85.1	$450,036	87.9
Food Processing	29,587	13.5	21,712	12.2	91,010	14.9	61,852	12.1
Total	$218,720	100.0 %	$177,793	100.0 %	$612,147	100.0 %	$511,888	100.0 %

Results of Operations

The following table sets forth certain consolidated statements of earnings items as a percentage of net sales for the periods.

	Three Months Ended		Nine Months Ended	
	Oct 1, 2011	Oct 2, 2010	Oct 1, 2011	Oct 2, 2010
Net sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales	60.1	60.2	60.1	60.2
Gross profit	39.9	39.8	39.9	39.8
Selling, general and administrative expenses	22.9	21.8	22.9	22.6
Income from operations	17.0	18.0	17.0	17.2
Net interest expense and deferred financing amortization	1.1	1.2	1.1	1.3
Other (income) expense, net	(0.2)	(0.1)	0.2	0.1
Earnings before income taxes	16.1	16.9	15.7	15.8
Provision for income taxes	5.4	5.3	5.7	5.7
Net earnings	10.7 %	11.6 %	10.0 %	10.1 %

Three Months Ended October 1, 2011 Compared to Three Months Ended October 2, 2010

NET SALES. Net sales for the third quarter of fiscal 2011 were $218.7 million as compared to $177.8 million in the third quarter of 2010.

- Net sales at the Commercial Foodservice Equipment Group amounted to $189.1 million in the third quarter of 2011 as compared to $156.1 million in the prior year quarter. Net sales resulting from the acquisitions of Beech and Lincat, which were acquired on April 12, 2011 and May 27, 2011, respectively, accounted for an increase of $17.3 million during the third quarter of 2011. Excluding the impact of these acquisitions, net sales of Commercial Foodservice Equipment increased by $15.7 million in the third quarter of 2011. The improvement in net sales reflects an improvement in market conditions as commercial restaurant customers increased their spending on replacement of equipment. Additionally, net sales reflects increased market penetration resulting from new product introductions and increased sales activities focused on major restaurant chain accounts and the emerging markets.

- Net sales for the Food Processing Equipment Group amounted to $29.6 million in the third quarter of 2011 as compared to $21.7 million in the prior year quarter. Net sales resulting from the acquisitions of Cozzini, Danfotech, Maurer and Auto-Bake, which were acquired on September 21, 2010, July 5, 2011, July 22, 2011 and August 1, 2011, respectively, accounted for an increase of $13.2 million. Excluding the impact of these acquisitions, net sales of Food Processing Equipment decreased by $5.3 million due to timing of customer orders.

GROSS PROFIT. Gross profit increased to $87.3 million in the third quarter of 2011 from $70.7 million in the prior year period, reflecting the impact of higher sales volumes. The gross margin rate was 39.9% in the third quarter of 2011 as compared to 39.8% in the prior year quarter. The net increase in the gross margin rate reflects:

- Improved margins resulting from acquisition integration initiatives including costs savings from plant consolidations.
- The benefit of increased sales volumes.
- Lower margins at the most recent acquisitions completed during fiscal 2011.
- Less favorable sales mix.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Combined selling, general, and administrative expenses increased from $38.7 million in the third quarter of 2010 to $50.1 million in the third quarter of 2011. As a percentage of net sales, operating expenses increased from 21.8% in the third quarter of 2010 to 22.9% in the third quarter of 2011. Selling expenses increased from $17.8 million in the third quarter of 2010 to $24.6 million in the third quarter of 2011. Selling expenses reflect increased costs of $5.4 million associated with the Cozzini, Beech, Lincat, Danfotech, Maurer and Auto-Bake acquisitions and $1.1 million associated with trade show and marketing related expenses. General and administrative expenses increased from $20.9 million in the third quarter of 2010 to $25.6 million in the third quarter of 2011. General and administrative expenses reflect $3.1 million of increased costs associated with the Cozzini, Beech, Lincat, Danfotech, Maurer and Auto-Bake acquisitions and $1.3 million of increased professional fees associated primarily with acquisition related activities.

NON-OPERATING EXPENSES. Interest and deferred financing amortization costs increased to $2.3 million in the third quarter of 2011 as compared to $2.2 million in the third quarter of 2010. Other income was $0.4 million in the third quarter of 2011 as compared to $0.1 million in the prior year third quarter.

INCOME TAXES. A tax provision of $11.8 million, at an effective rate of 34%, was recorded during the third quarter of 2011, as compared to a $9.4 million provision at a 31% effective rate in the prior year quarter. The prior year effective rate included a one-time benefit associated with the deduction of transaction costs related to the acquisition activities, favorable adjustments to tax reserves related to reduced state exposures, and increased deductions for qualified manufacturing activities.

Nine Months Ended October 1, 2011 Compared to Nine Months Ended October 2, 2010

NET SALES. Net sales for the nine-month period ended October 1, 2011 were $612.1 million as compared to $511.9 million in the nine-month period ended October 2, 2010.

- Net sales at the Commercial Foodservice Equipment Group for the nine-month period ended October 1, 2011 amounted to $521.1 million as compared to $450.0 million for the nine-month period ended October 2, 2010. Net sales resulting from the acquisitions of PerfectFry, Beech and Lincat, which were acquired on July 13, 2010, April 12, 2011 and May 27, 2011, respectively, accounted for an increase of $25.7 million during the nine-month period ended October 1, 2011. Excluding the impact of these acquisitions, net sales of Commercial Foodservice Equipment for the nine-month period ended October 1, 2011 increased by $45.4 million as compared to the nine-month period ended October 2, 2010. The improvement in net sales reflects an improvement in market conditions as commercial restaurant customers increased their spending on replacement of equipment. Additionally, the increase in net sales reflects increased market penetration resulting from new product introductions and increased sales activities focused on major restaurant chain accounts and the emerging markets.

- Net sales for the Food Processing Equipment Group amounted to $91.0 million in the nine-month period ended October 1, 2011 as compared to $61.9 million in the prior year period. Net sales resulting from the acquisitions of Cozzini, Danfotech, Maurer and Auto-Bake, which were acquired on September 21, 2010, July 5, 2011, July 22, 2011 and August 1, 2011, respectively, accounted for an increase of $35.4 million. Excluding the impact of this acquisition, net sales of Food Processing Equipment decreased by $6.3 million due to timing of customer orders.

GROSS PROFIT. Gross profit increased to $244.5 million in the third quarter of 2011 from $203.6 million in the prior year period, reflecting the impact of higher sales volumes. The gross margin rate was 39.9% in the nine-month period ended October 1, 2011 as compared to 39.8% in the prior year period. The net increase in the gross margin rate reflects:

- The benefit of increased sales volumes.
- Improved margins at certain of the newly acquired operating companies which have improved due to acquisition integration initiatives including costs savings from plant consolidations, partially offset by;
- The impact of rising material costs.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Combined selling, general, and administrative expenses increased from $115.4 million in the nine-month period ending October 2, 2010 to $140.7 million in the nine-month period ended October 1, 2011. As a percentage of net sales, operating expenses increased from 22.6% in the nine-month period ended October 2, 2010 to 22.9% in the nine-month period ended October 1, 2011. Selling expenses increased from $54.4 million in the nine-month period ended October 2, 2010 to $66.7 million in the nine-month period ended October 1, 2011. Selling expenses reflect increased costs of $9.8 million associated with the Cozzini, Beech, Lincat, Danfotech, Maurer and Auto-Bake acquisitions, $1.2 million associated with trade show expenses and $0.8 million associated with commission expense due to higher sales volumes. General and administrative expenses increased from $61.0 million in the nine-month period ended October 2, 2010 to $74.0 million in the nine-month period ended October 1, 2011. General and administrative expenses reflect $7.1 million of increased costs associated with the Cozzini, Beech, Lincat, Danfotech, Maurer and Auto-Bake acquisitions and $3.4 million of increased professional services associated primarily with acquisition related activities.

NON-OPERATING EXPENSES. Interest and deferred financing amortization costs decreased to $6.5 million in nine-month period ended October 1, 2011 as compared to $6.9 million in the nine-month period ended October 2, 2010, due to lower interest rates on lower average debt balances. Other expense was $1.0 million in the nine-month period ended October 1, 2011 as compared to $0.4 million in the nine-month period ended October 2, 2010 and due primarily to higher foreign exchange transaction losses.

INCOME TAXES. A tax provision of $35.4 million, at an effective rate of 37%, was recorded during the nine-month period ended October 1, 2011, as compared to a $29.0 million provision at a 36% effective rate in the nine-month period ended October 2, 2010.

Financial Condition and Liquidity

During the nine months ended October 1, 2011, cash and cash equivalents increased by $5.7 million to $13.4 million at October 1, 2011 from $7.7 million at January 1, 2011. Net borrowings increased from $214.0 million at January 1, 2011 to $303.6 million at October 1, 2011.

OPERATING ACTIVITIES. Net cash provided by operating activities was $65.7 million for the nine-month period ended October 1, 2011 compared to $66.2 million for the nine-month period ended October 2, 2010.

During the nine months ended October 1, 2011, working capital levels changed due to increased working capital needs. These changes in working capital levels included a $9.0 million increase in inventory, due to several factors including increased order rates, increased inventory levels during build out periods in conjunction with plant consolidation efforts and higher levels of stock associated with foreign sourcing initiatives. Accounts receivable also increased $11.7 million due to higher sales volumes. Changes in working capital levels also included a $2.3 million decrease in prepaid expenses and other assets, $9.3 million decrease in accounts payable and a $6.0 million increase in accrued expenses and other non-current liabilities.

INVESTING ACTIVITIES. During the nine months ended October 1, 2011, net cash used in investing activities amounted to $136.1 million. This included $127.5 million of current period acquisitions, which included $13.0 million, $82.1 million, $6.1 million, $3.8 million and $22.5 million in connection with the acquisitions of Beech, Lincat Danfotech, Maurer and Auto-Bake, respectively. Investing activities also include deferred payments of $3.7 million related to the Giga, Cooktek and Cozzini acquisitions completed in prior years. The company also had net capital expenditures of $4.9 million primarily associated with additions and upgrades of production equipment.

FINANCING ACTIVITIES. Net cash flows provided by financing activities were $76.3 million during the nine months ended October 1, 2011. The company's borrowing activities included $88.0 million of net proceeds under its $600.0 million revolving credit facility and $1.5 million of net proceeds of foreign borrowings. During the second quarter of 2011, the company exercised a provision under its current credit facility that allowed the company to increase the amount of availability under the revolving credit line by approximately $102.0 million. Related to restricted stock vestings during the first quarter of 2011, the company also used $9.5 million to repurchase 113,550 shares of its common stock that were surrendered to the company by employees in lieu of cash for payment of withholding taxes. Additionally, the company used $3.5 million to repurchase 51,768 shares of its common stock under its treasury stock buyback program.

At October 1, 2011, the company was in compliance with all covenants pursuant to its borrowing agreements. The company believes that its current capital resources, including cash and cash equivalents, cash generated from operations, funds available from its revolving credit facility and access to the credit and capital markets will be sufficient to finance its operations, debt service obligations, capital expenditures, acquisitions, product development and integration expenditures for the foreseeable future.

Recently Issued Accounting Standards

In December 2010, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2010-29, "Business Combinations (Topic 805)." ASU No. 2010-29 clarifies the disclosures required for pro forma information for business combinations. ASU No. 2010-29 specifies if comparative financial statements are presented, revenue and earnings of a combined entity should be disclosed as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments in ASU 2010-29 are effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The company adopted the provisions of ASU No. 2010-29 on January 2, 2011. As the company had no material acquisitions during the nine months ended October 1, 2011, there were no disclosures required.

In May 2011, the FASB issued ASU No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." This update provides clarification on existing fair value measurement requirements, amends existing guidance primarily related to fair value measurements for financial instruments, and requires enhanced disclosures on fair value measurements. The additional disclosures are specific to Level 3 fair value measurements, transfers between Level 1 and Level 2 of the fair value hierarchy, financial instruments not measured at fair value and use of an asset measured or disclosed at fair value differing from its highest and best use. This ASU is effective for interim and annual periods beginning after December 15, 2011, and will be applied prospectively. The adoption of this guidance is not expected to affect the company's financial position, results of operations or cash flows.

In June 2011, the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income," which eliminates the option to present the components of other comprehensive income in the statement of changes in stockholders' equity. Instead, entities will have the option to present the components of net income, the components of other comprehensive income and total comprehensive income in a single continuous statement or in two separate but consecutive statements. The guidance does not change the items reported in other comprehensive income or when an item of other comprehensive income is reclassified to net income. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, and will be applied retrospectively. As this guidance only revises the presentation of comprehensive income, the adoption of this guidance is not expected to affect the company's financial position, results of operations or cash flows.

In September 2011, the FASB issued ASU No. 2011-08, “Intangibles – Goodwill and Other (Topic 350),” This ASU will allow an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it should calculate the fair value of a reporting unit. The ASU also amends previous guidance by expanding upon the examples of events and circumstances that an entity should consider between annual impairment tests in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Also, the ASU provides additional examples of events and circumstances that an entity having a reporting unit with a zero or negative carrying amount should consider in determining whether to measure an impairment loss, if any, under the second step of the goodwill impairment test. This ASU is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity’s financial statements for the most recent annual or interim period have not yet been issued. The company is evaluating the impact the application of this ASU will have on the company’s financial position, results of operations and cash flows.

Critical Accounting Policies and Estimates

Management's discussion and analysis of financial condition and results of operations are based upon the company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses as well as related disclosures. On an ongoing basis, the company evaluates its estimates and judgments based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Revenue Recognition. The company recognizes revenue on the sale of its products when risk of loss has passed to the customer, which occurs at the time of shipment, and collectibility is reasonably assured. The sale prices of the products sold are fixed and determinable at the time of shipment. Sales are reported net of sales returns, sales incentives and cash discounts based on prior experience and other quantitative and qualitative factors.

At the Food Processing Equipment Group, the company enters into long-term sales contracts for certain products. Revenue under these long-term sales contracts is recognized using the percentage of completion method defined within ASC 605-35 “Construction-Type and Production-Type Contracts” due to the length of time to fully manufacture and assemble the equipment. The company measures revenue recognized based on the ratio of actual labor hours incurred in relation to the total estimated labor hours to be incurred related to the contract. Because estimated labor hours to complete a project are based upon forecasts using the best available information, the actual hours may differ from original estimates. The percentage of completion method of accounting for these contracts most accurately reflects the status of these uncompleted contracts in the company's financial statements and most accurately measures the matching of revenues with expenses. At the time a loss on a contract becomes known, the amount of the estimated loss is recognized in the consolidated financial statements.

Property and equipment. Property and equipment are depreciated or amortized on a straight-line basis over their useful lives based on management's estimates of the period over which the assets will be utilized to benefit the operations of the company. The useful lives are estimated based on historical experience with similar assets, taking into account anticipated technological or other changes. The company periodically reviews these lives relative to physical factors, economic factors and industry trends. If there are changes in the planned use of property and equipment or if technological changes were to occur more rapidly than anticipated, the useful lives assigned to these assets may need to be shortened, resulting in the recognition of increased depreciation and amortization expense in future periods.

Long-lived assets. Long-lived assets (including goodwill and other intangibles) are reviewed for impairment annually and whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In assessing the recoverability of the company's long-lived assets, the company considers changes in economic conditions and makes assumptions regarding estimated future cash flows and other factors. Estimates of future cash flows are judgments based on the company's experience and knowledge of operations. These estimates can be significantly impacted by many factors including changes in global and local business and economic conditions, operating costs, inflation, competition, and consumer and demographic trends. If the company's estimates or the underlying assumptions change in the future, the company may be required to record impairment charges.

Warranty. In the normal course of business the company issues product warranties for specific product lines and provides for the estimated future warranty cost in the period in which the sale is recorded. The estimate of warranty cost is based on contract terms and historical warranty loss experience that is periodically adjusted for recent actual experience. Because warranty estimates are forecasts that are based on the best available information, claims costs may differ from amounts provided. Adjustments to initial obligations for warranties are made as changes in the obligations become reasonably estimable.

Litigation. From time to time, the company is subject to proceedings, lawsuits and other claims related to products, suppliers, employees, customers and competitors. The company maintains insurance to partially cover product liability, workers compensation, property and casualty and general liability matters. The company is required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of accrual required, if any, for these contingencies is made after assessment of each matter and the related insurance coverage. The accrual requirements may change in the future due to new developments or changes in approach such as a change in settlement strategy in dealing with these matters. The company does not believe that any pending litigation will have a material adverse effect on its financial condition or results of operations.

Income taxes. The company operates in numerous foreign and domestic taxing jurisdictions where it is subject to various types of tax, including sales tax and income tax. The company's tax filings are subject to audits and adjustments. Because of the nature of the company’s operations, the nature of the audit items can be complex and the objectives of the government auditors can result in a tax on the same transaction or income in more than one state or country. As part of the company's calculation of the provision for taxes, the company establishes reserves for the amount that it expects to incur as a result of audits. The reserves may change in the future due to new developments related to the various tax matters.

Contractual Obligations

The company's contractual cash payment obligations as of October 1, 2011 are set forth below (in thousands):

	Amounts Due to Sellers From Acquisitions	Long-term Debt	Operating Leases	Idle Facility Leases	Total Contractual Cash Obligations
Less than 1 year	$ 819	$ 6,771	$ 3,798	$ 470	$ 11,858
1-3 years	1,983	295,494	3,720	733	301,930
3-5 years	-	268	1,283	243	1,794
After 5 years	-	1,106	1,226	-	2,332
	$ 2,802	$ 303,639	$ 10,027	$ 1,446	$ 317,914

The company has obligations to make $2.8 million of purchase price payments to the sellers of CookTek that were deferred in conjunction with the acquisition.

The company has contractual obligations under its various debt agreements to make interest payments. These amounts are subject to the level of borrowings in future periods and the interest rate for the applicable periods, and therefore the amounts of these payments is not determinable.

The company has $6.3 million in outstanding letters of credit, which expire on October 1, 2012, to secure potential obligations under various business programs.

Idle facility leases consist of obligations for manufacturing locations that were exited in conjunction with the company's manufacturing consolidation efforts. These lease obligations continue through June 2015. The obligations presented above do not reflect any anticipated sublease income from the facilities.

The projected benefit obligation of the company’s defined benefit plans exceeded the plans’ assets by $11.5 million at the end of 2010. The unfunded benefit obligations were comprised of a $3.7 million underfunding of the company’s Smithville plan, which was acquired as part of the Star acquisition, $0.8 million underfunding of the company's Elgin union plan and $7.0 million of underfunding of the company's director plans. The company does not expect to contribute to the director plans in 2011. The company expects to continue to make minimum contributions to the Smithville and Elgin plan as required by the Employee Retirement Income Security Act of 1974, which are expected to be $0.3 million and $0.1 million, respectively in 2011.

The company places purchase orders with its suppliers in the ordinary course of business. These purchase orders are generally to fulfill short-term manufacturing requirements of less than 90 days and most are cancelable with a restocking penalty. The company has no long-term purchase contracts or minimum purchase obligations with any supplier.

The company has no activities, obligations or exposures associated with off-balance sheet arrangements.

Item 3. Quantitative and Qualitative Disclosures About MarketRisk

Interest Rate Risk

The company is exposed to market risk related to changes in interest rates. The following table summarizes the maturity of the company's debt obligations.

Twelve Month Period Ending	Fixed Rate Debt	Variable Rate Debt
	(in thousands)	
October 1, 2012	$ —	$ 6,771
October 1, 2013	—	295,370
October 1, 2014	—	124
October 1, 2015	—	131
October 1, 2016 and thereafter	—	1,243
	$ —	$ 303,639

During the second quarter of 2011, the company exercised a provision under its current credit facility that allowed the company to increase the amount of availability under the revolving credit line by approximately $102.0 million. Terms of the company's senior credit agreement provide for $600.0 million of availability under a revolving credit line. As of October 1, 2011, the company had $295.3 million of borrowings outstanding under this facility. The company also has $6.3 million in outstanding letters of credit as of October 1, 2011, which reduces the borrowing availability under the revolving credit line. Remaining borrowing availability under this facility, which is also reduced by the company's foreign borrowings, was $290.0 million at October 1, 2011.

At October 1, 2011, borrowings under the senior secured credit facility are assessed at an interest rate 1.0% above LIBOR for long-term borrowings or at the higher of the Prime rate and the Federal Funds Rate. At October 1, 2011 the average interest rate on the senior debt amounted to 1.32%. The interest rates on borrowings under the senior secured credit facility may be adjusted quarterly based on the company's indebtedness ratio on a rolling four-quarter basis. Additionally, a commitment fee, based upon the indebtedness ratio is charged on the unused portion of the revolving credit line. This variable commitment fee amounted to 0.2% as of October 1, 2011.

In August 2006, the company completed its acquisition of Houno A/S in Denmark. This acquisition was funded in part with locally established debt facilities with borrowings in Danish Krone. On October 1, 2011 these facilities amounted to $3.5 million in U.S. dollars, including $1.8 million outstanding under a revolving credit facility and $1.7 million of a term loan. The interest rate on the revolving credit facility is assessed at 1.25% above Euro LIBOR, which amounted to 3.9% on October 1, 2011. The term loan matures in 2013 and the interest rate is assessed at 4.55%.

In April 2008, the company completed its acquisition of Giga Grandi Cucine S.r.l in Italy. This acquisition was funded in part with locally established debt facilities with borrowings denominated in Euro. On October 1, 2011 these facilities amounted to $4.9 million in U.S. dollars. The interest rate on the credit facilities is tied to nine-month Euro LIBOR. At October 1, 2011, the average interest rate on these facilities was approximately 3.0%. The facilities mature in April of 2015.

The company believes that its current capital resources, including cash and cash equivalents, cash generated from operations, funds available from its revolving credit facility and access to the credit and capital markets will be sufficient to finance its operations, debt service obligations, capital expenditures, product development and integration expenditures for the foreseeable future.

The company has historically entered into interest rate swap agreements to effectively fix the interest rate on a portion of its outstanding debt. The agreements swap one-month LIBOR for fixed rates. As of October 1, 2011 the company had the following interest rate swaps in effect:

Notional Amount	Fixed Interest Rate	Effective Date	Maturity Date
$ 15,000,000	1.220 %	11/23/09	11/23/11
20,000,000	1.800 %	11/23/09	11/23/12
20,000,000	1.560 %	03/11/10	12/11/12
10,000,000	1.120 %	03/11/10	03/11/12
15,000,000	0.950 %	08/06/10	12/06/12
25,000,000	1.610 %	02/23/11	02/24/14
25,000,000	2.520 %	02/23/11	02/23/16
25,000,000	0.975 %	07/18/11	07/18/14
15,000,000	1.150 %	09/12/11	09/12/16
15,000,000	0.620 %	09/12/11	09/11/14

The terms of the senior secured credit facility limit the paying of dividends, capital expenditures and leases, and require, among other things, a maximum ratio of indebtedness to earnings before interest, taxes, depreciation and amortization ("EBITDA") of 3.5 and a minimum EBITDA to fixed charges ratio of 1.25. The credit agreement also provides that if a material adverse change in the company's business operations or conditions occurs, the lender could declare an event of default. Under terms of the agreement a material adverse effect is defined as (a) a material adverse change in, or a material adverse effect upon, the operations, business properties, condition (financial and otherwise) or prospects of the company and its subsidiaries taken as a whole; (b) a material impairment of the ability of the company to perform under the loan agreements and to avoid any event of default; or (c) a material adverse effect upon the legality, validity, binding effect or enforceability against the company of any loan document. A material adverse effect is determined on a subjective basis by the company's creditors. The credit facility is secured by the capital stock of the company's domestic subsidiaries, 65% of the capital stock of the company's foreign subsidiaries and substantially all other assets of the company. At October 1, 2011, the company was in compliance with all covenants pursuant to its borrowing agreements.

Financing Derivative Instruments

The company has entered into interest rate swaps to fix the interest rate applicable to certain of its variable-rate debt. The agreements swap one-month LIBOR for fixed rates. The company has designated these swaps as cash flow hedges and all changes in fair value of the swaps are recognized in accumulated other comprehensive income. As of October 1, 2011, the fair value of these instruments was a loss of $3.5 million. The change in fair value of these swap agreements in the first nine months of 2011 was a loss of $1.3 million, net of taxes.

Foreign Exchange Derivative Financial Instruments

The company uses foreign currency forward purchase and sale contracts with terms of less than one year to hedge its exposure to changes in foreign currency exchange rates. The company's primary hedging activities are to mitigate its exposure to changes in exchange rates on intercompany and third party trade receivables and payables. The company does not currently enter into derivative financial instruments for speculative purposes. In managing its foreign currency exposures, the company identifies and aggregates naturally occurring offsetting positions and then hedges residual balance sheet exposures. The following table summarizes the forward contracts outstanding at October 1, 2011. The fair value of the forward contracts was a gain of less than $0.1 million at the end of the third quarter of 2011.

Sell	Purchase	Maturity
15,000,000 British Pounds	17,172,000 Euro Dollars	October 4, 2011
14,000,000 British Pounds	16,037,000 Euro Dollars	October 4, 2011
3,000,000 Euro Dollars	4,270,000 US Dollars	December 30, 2011
1,500,000 British Pounds	2,376,000 US Dollars	December 30, 2011

Item 4. Controls and Procedures

The company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

As of October 1, 2011, the company carried out an evaluation, under the supervision and with the participation of the company's management, including the company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the company's disclosure controls and procedures. Based on the foregoing, the company's Chief Executive Officer and Chief Financial Officer concluded that the company's disclosure controls and procedures were effective as of the end of this period.

During the quarter ended October 1, 2011, there has been no change in the company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

PART II. OTHER INFORMATION

The company was not required to report the information pursuant to Items 1 through 6 of Part II of Form 10-Q for the three months ended October 1, 2011, except as follows:

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

c) Issuer Purchases of Equity Securities

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program	Maximum Number of Shares that May Yet be Purchased Under the Plan or Program
July 3 to July 30, 2011	—	—	—	349,885
July 31 to August 27, 2011	—	—	—	349,885
August 28, 2011 to October 1, 2011	51,768	69.10	51,768	298,117
Quarter ended October 1, 2011	51,768	69.10	51,768	298,117

In July 1998, the company's Board of Directors adopted a stock repurchase program that authorized the purchase of common shares in open market purchases. As of October 1, 2011, 1,501,883 shares had been purchased under the 1998 stock repurchase program.

Item 6. Exhibits

Exhibits – The following exhibits are filed herewith:

Exhibit 31.1	Rule 13a-14(a)/15d -14(a) Certification of the Chief Executive Officer as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 31.2	Rule 13a-14(a)/15d -14(a) Certification of the Chief Financial Officer as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.1	Certification by the Principal Executive Officer of The Middleby Corporation Pursuant to Rule 13A-14(b) under the Exchange Act and Section 906 of the Sarbanes-Oxley Act of 2002(18 U.S.C. 1350).
Exhibit 32.2	Certification by the Principal Financial Officer of The Middleby Corporation Pursuant to Rule 13A-14(b) under the Exchange Act and Section 906 of the Sarbanes-Oxley Act of 2002(18 U.S.C. 1350).
Exhibit 101	Financial statements on Form 10-Q for the quarter ended October 1, 2011, filed on November 10, 2011, formatted in Extensive Business Reporting Language (XBRL); (i) condensed consolidated balance sheets, (ii) condensed consolidated statements of earnings, (iii) condensed statements of cash flows, (iv) notes to the condensed consolidated financial statements.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE MIDDLEBY CORPORATION
(Registrant)

Date November 10, 2011

By: /s/ Timothy J. FitzGerald
Timothy J. FitzGerald
Vice President,
Chief Financial Officer