

POWELL INDUSTRIES INC

Form 10-K

December 08, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K**

(Mark One)

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the fiscal year ended September 30, 2010
OR**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

**Commission File Number 001-12488
Powell Industries, Inc.**
(Exact name of registrant as specified in its charter)

Delaware
*(State or other jurisdiction of
incorporation or organization)*
**8550 Mosley RD
Houston, Texas**
(Address of principal executive offices)

88-0106100
*(I.R.S. Employer
Identification No.)*
77075-1180
(Zip Code)

**Registrant's telephone number, including area code:
(713) 944-6900**

**Securities registered pursuant to section 12(b) of the Act:
Common Stock, par value \$.01 per share**

**Securities registered pursuant to Section 12(g) of Act:
None**

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

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

to submit and post such files). Yes No

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant as of the last business day of the most recently completed second fiscal quarter, March 31, 2010, was approximately \$376,593,000.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

At December 3, 2010, there were 11,689,607 outstanding shares of the registrant's common stock, par value \$0.01 per share.

Documents Incorporated By Reference

Portions of the registrant's definitive Proxy Statement for the 2011 annual meeting of stockholders to be filed not later than 120 days after September 30, 2010, are incorporated by reference into Part III of this Form 10-K.

POWELL INDUSTRIES, INC.

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**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS;
RISK FACTORS**

Forward-Looking Statements

This Annual Report on Form 10-K (Annual Report) includes forward-looking statements based on our current expectations, which are subject to risks and uncertainties. Forward-looking statements include information concerning future results of operations and financial condition. Statements that contain words such as believes, expects, anticipates, intends, estimates, continue, should, could, may, plan, project, predict, will or similar forward-looking statements. These forward-looking statements are subject to risks and uncertainties, and many factors could affect the future financial results and condition of the Company. Factors that may have a material effect on our revenues, expenses and operating results include adverse business or market conditions, our ability to secure and satisfy customers, our customers' financial condition and their ability to secure financing to support current and future projects, the availability and cost of materials from suppliers, adverse competitive developments and changes in customer requirements as well as those circumstances discussed under Item 1A. Risk Factors, below. Accordingly, actual results may differ materially from those expressed or implied by the forward-looking statements contained in this Annual Report. Any forward-looking statements made by or on our behalf are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

The forward-looking statements contained in this Annual Report are based on current assumptions that we will continue to develop, market, manufacture and ship products and provide services on a competitive and timely basis; that competitive conditions in our markets will not change in a materially adverse way; that we will accurately identify and meet customer needs for products and services; that we will be able to retain and hire key employees; that our products and capabilities will remain competitive; that the financial markets and banking systems will stabilize and availability of credit will continue; that risks related to shifts in customer demand are minimized and that there will be no material adverse change in the operations or business of the Company. Assumptions relating to these factors involve judgments that are based on available information, which may not be complete, and are subject to changes in many factors beyond the Company's control that can materially affect results. Because of these and other factors that affect our operating results, past financial performance should not be considered an indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

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PART I

Item 1. *Business*

Overview

Powell Industries, Inc. (we, us, our, Powell or the Company) was incorporated in the state of Delaware in 2004 as a successor to a Nevada company incorporated in 1968. The Nevada corporation was the successor to a company founded by William E. Powell in 1947, which merged into the Company in 1977. Our major subsidiaries, all of which are wholly-owned, include: Powell Electrical Systems, Inc.; Transdyn, Inc.; Powell Industries International, Inc.; Switchgear & Instrumentation Limited (S&I) and Powell Canada Inc.

We develop, design, manufacture and service custom engineered-to-order equipment and systems for the management and control of electrical energy and other critical processes. Headquartered in Houston, Texas, we serve the transportation, environmental, energy, industrial and utility industries.

Our website address is www.powellind.com. We make available, free of charge on or through our website, copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (SEC). Paper or electronic copies of such material may also be requested by contacting the Company at our corporate offices.

On December 13, 2005, we announced a change in our fiscal year-end from October 31 to September 30, effective September 30, 2006. The change was designed to align our financial reporting with calendar quarters and to reduce the impact holidays have on our reporting timeline.

Our business operations are consolidated into two business segments: Electrical Power Products and Process Control Systems. Approximately 71%, 77% and 73% of our consolidated revenues for the fiscal years ended September 30, 2010, 2009 and 2008, respectively, were generated in the United States of America. Approximately 79% of our long-lived assets were located in the United States at September 30, 2010, with the remaining balance located primarily in the United Kingdom and Canada. Financial information related to our business and geographical segments is included in Note N of Notes to Consolidated Financial Statements.

On December 15, 2009, we acquired the business and certain assets of PowerComm Inc. and its subsidiaries, Redhill Systems Ltd., Nextron Corporation, PCG Technical Services Inc. and Concorde Metal Manufacturing Ltd (the entire business of which is referred to herein as Powell Canada) for \$23.4 million, not including expenses. Powell Canada is headquartered in Edmonton, Alberta, Canada, and provides electrical and maintenance services in western Canada. Powell Canada is also a manufacturer of switchgear and related products, primarily serving the oil and gas industry in western Canada. The operating results of Powell Canada are included in our Electrical Power Products business segment from the acquisition date. In conjunction with the acquisition of Powell Canada, on April 1, 2010, we finalized the acquisition of a 50% ownership in a joint venture in Kazakhstan. The Company has made a strategic decision to exit this joint venture. For further information on the Powell Canada acquisition, see Note D of Notes to Consolidated Financial Statements.

On August 7, 2006, we purchased certain assets related to the manufacturing of American National Standards Institute (ANSI) medium-voltage switchgear and circuit breaker business of General Electric Company's (GE) Consumer & Industrial unit for \$32.0 million, not including expenses. We refer to the acquired product line herein as Power/Vac®. The operating results of Power/Vac® are included in our Electrical Power Products business segment from the acquisition date.

On July 14, 2006, we acquired certain assets and hired the service and administrative employees of an electrical services company in Louisiana for approximately \$1.5 million. The purchase price was paid from existing cash and short-term marketable securities. The operating results of this acquisition are included in our Electrical Power Products business segment from the acquisition date.

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Electrical Power Products

Our Electrical Power Products business segment designs, develops, manufactures and markets custom engineered-to-order electrical power distribution and control systems designed (1) to distribute, monitor and control the flow of electrical energy and (2) to provide protection to motors, transformers and other electrically-powered equipment. Our principal products include power control room substation packages, traditional and arc-resistant distribution switchgear, medium-voltage circuit breakers, offshore generator and control modules, monitoring and control communications systems, motor control centers and bus duct systems. These products are designed for application voltages ranging from 480 volts to in excess of 38,000 volts and are used in electric rail transportation, refining, chemical, offshore oil and gas production, electric utility and other heavy industrial markets. Our product scope includes designs tested to meet both U.S. standards (ANSI) and international design standards (IEC International Electrotechnical Commission). We also seek to assist customers by providing value-added services such as spare parts, field service inspection and repair, retrofit and retrofill components for existing systems and replacement circuit breakers for switchgear that is obsolete or that is no longer produced by the original manufacturer. We work to establish long-term relationships with the end users of our systems and with the design and construction engineering firms contracted by those end users.

Customers and Markets

This business segment's principal products are designed for use by and marketed to technologically sophisticated users of large amounts of electrical energy that typically have a need for complex combinations of electrical components and systems. Our customers and their industries include oil and gas producers, oil and gas pipelines, refineries, petrochemical plants, electrical power generators, public and private utilities, co-generation facilities, mining/metals operations, pulp and paper plants, transportation authorities, governmental agencies and other large industrial customers.

Products and services are principally sold directly to the end-user or to an engineering, procurement and construction (EPC) firm on behalf of the end-user. Each project is specifically tailored to meet the exact specifications and requirements of the individual customer. Powell's expertise is in the engineering and packaging of the various systems into a single deliverable. We market and sell our products and services to a wide variety of customers, markets and geographic regions. Contracts may represent large-scale projects with an individual customer. By their nature, these projects are typically nonrecurring. Thus, multiple and/or continuous projects of similar magnitude with the same customer may vary. As such, gaps in large project awards may cause material fluctuations in segment revenues.

We could be adversely impacted by a significant reduction in business volume from a particular industry which we currently serve. As a result of the supply agreement that we entered into on August 7, 2006, with GE, our revenues from GE were approximately \$58 million, \$86 million and \$82 million in fiscal 2010, fiscal 2009 and fiscal 2008, respectively, or approximately 11%, 14% and 13% of our consolidated revenues for these periods. Aside from GE, with whom we have a long-term supply agreement, we do not believe that the loss of any specific customer would have a material adverse effect on our business. GE has become a significant customer and has accounted for, and could continue to account for, more than 10% of the annual revenues of this business segment as a result of the supply agreement that we entered into on August 7, 2006.

During each of the past three fiscal years, no one country outside of the United States accounted for more than 10% of segment revenues. For information on the geographic areas in which our consolidated revenues were recorded in each of the past three fiscal years, see Note N of Notes to Consolidated Financial Statements.

Competition

We strive to be the supplier of choice for custom engineered system solutions and services to a variety of customers and markets. Our activities are predominantly in the oil and gas and the electric utility industries, but also include other markets where customers need to manage, monitor and control large amounts of electrical energy. The majority of our business is in support of capital investment projects which are competitively bid. We compete with a small number of multinational competitors that sell to a broad industrial and geographic market and with smaller, regional competitors that typically have limited capabilities and scope of supply.

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Our principal competitors include ABB, Eaton Corporation, GE, Schneider Electric and Siemens. The competitive factors used during bid evaluation by our customers vary from project to project and may include technical support and application expertise, engineering and manufacturing capabilities, equipment rating, delivered value, scheduling and price. A significant portion of our business is from repeat customers and many times involves third-party engineering and construction companies hired by the end-user and with which we also have long and established relationships. We consider our engineering, manufacturing and service capabilities vital to the success of our business, and believe our technical and project management strengths, together with our responsiveness and flexibility to the needs of our customers, give us a competitive advantage in our markets. Ultimately, our competitive position is dependent upon our ability to provide quality custom engineered-to-order products, services and systems on a timely basis at a competitive price.

Backlog

Backlog represents the dollar amount of revenue that we expect to realize from work to be performed on uncompleted contracts, including new contractual agreements on which work has not begun. Our methodology for determining backlog may not be comparable to the methodology used by other companies. Orders included in our backlog are represented by customer purchase orders and contracts, which we believe to be firm. Orders in the Electrical Power Products business segment backlog at September 30, 2010, totaled \$245.4 million compared to \$329.6 million at September 30, 2009. Our backlog has declined due to the ongoing economic downturn which has lead our customers to reduce and delay spending on new capital projects. We anticipate that approximately \$242.6 million of our ending fiscal 2010 backlog will be fulfilled during our fiscal year 2011. Conditions outside of our control have caused us to experience some customer delays and cancellations of certain projects in the past; accordingly, backlog may not be indicative of future operating results as orders in our backlog may be cancelled or modified by our customers.

Raw Materials and Suppliers

The principal raw materials used in Electrical Power Products operations include steel, copper, aluminum and various electrical components. These raw material costs represented approximately 45% of our revenues in fiscal 2010. Unanticipated increases in raw material requirements, disruptions in supplies or price increases could increase production costs and adversely affect profitability.

We purchase certain key electrical components on a sole-sourced basis and maintain a qualification and performance monitoring program to control risk associated with sole-sourced items. Changes in our design to accommodate similar components from other suppliers could be implemented to resolve a supply problem related to a sole-sourced component. In this circumstance, supply problems could result in short-term delays in our ability to meet commitments to our customers. We believe that sources of supply for raw materials and components are generally sufficient, and we have no reason to believe a shortage of raw materials will cause any material adverse impact during fiscal year 2011. While we are not dependent on any one supplier for a material amount of our raw materials, we are highly dependent on our suppliers in order to meet commitments to our customers. We did not experience significant or unusual problems in the purchase of key raw materials and commodities in the past three years.

Inflation

This business segment is subject to the effects of changing prices. During the last three fiscal years, we experienced price volatility for certain commodities, in particular steel, copper and aluminum products, which are used in the production of our products. While the cost outlook for commodities used in the production of our products is not certain, we believe we can manage these inflationary pressures through contract pricing adjustments and by actively pursuing internal cost reduction efforts. We did not enter into any derivative contracts to hedge our exposure to commodity price changes in fiscal years 2010, 2009 or 2008.

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Employees

At September 30, 2010, the Electrical Power Products business segment had 2,430 full-time employees located in the United States, the United Kingdom, Canada and Singapore. Our employees are not represented by unions, and we believe that our relationship with our employees is good.

Research and Development

This business segment's research and development activities are directed toward the development of new products and processes as well as improvements in existing products and processes. Research and development expenditures were \$6.0 million, \$5.8 million and \$6.3 million in fiscal years 2010, 2009 and 2008, respectively, and are reported in selling, general and administrative expenses in the consolidated statement of operations.

Intellectual Property

While we are the holder of various patents, trademarks and licenses relating to this business segment, we do not consider any individual intellectual property to be material to our consolidated business operations.

Process Control Systems

Our Process Control Systems business segment designs and delivers custom engineered-to-order technology solutions that help our customers manage their critical transportation, environmental and energy management processes and facilities. Our proprietary DYNAC[®] software suite provides a highly integrated operations management solution for these vital operations. The mission-critical information may be traffic flow in our intelligent transportation management solutions, water quality in our environmental treatment solutions or electrical power status in the case of our substation automation solutions. DYNAC[®] has user configurable applications designed specifically for clients that require high performance, 24/7 availability and superior data integrity in a secure environment.

We provide a comprehensive set of technical services to deliver these systems. A diverse team of professional systems engineers, software engineers, analysts, network specialists and automation engineers provide expertise for the entire life cycle of a technology project. We have designed and built systems for various facilities and roadways around the world.

Customers and Markets

This business segment's products and services are principally sold directly to end-users in the transportation, environmental and energy sectors. From time to time, a significant percentage of revenues may result from one specific contract or customer due to the nature of large projects common to this business segment. In each of the past three fiscal years, revenues with one or more customers individually accounted for more than 10% of our segment revenues. Revenues from these customers totaled \$3.2 million, \$7.4 million and \$5.4 million in fiscal 2010, 2009 and 2008, respectively. Contracts often represent large-scale, single-need projects with an individual customer. By their nature, these projects are typically nonrecurring for a given customer. Thus, multiple and/or continuous projects of similar magnitude with the same customer are rare. As such, gaps in large project awards may cause material fluctuations in segment revenues.

During each of the past three fiscal years, the United States is the only country that accounted for more than 10% of segment revenues. For information on the geographic areas in which our consolidated revenues were recorded in each of the past three fiscal years, see Note N of Notes to Consolidated Financial Statements.

Competition

This business segment operates in a competitive market where competition for each contract varies. Depending upon the type of system and customer requirements, the competition may include large multinational firms as well as smaller regional competitors.

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Our customized systems are designed to meet the specifications of our customers. Each system is designed, delivered and installed to the specific requirements of the particular application. We consider our engineering, systems integration and technical support capabilities vital to the success of our business. We believe our turnkey systems integration capabilities, customizable software, domain expertise, specialty contracting experience and financial strength give us a competitive advantage in our markets.

Backlog

Backlog represents the dollar amount of revenue that we expect to realize from work to be performed on uncompleted contracts, including new contractual agreements on which work has not begun. Our methodology for determining backlog may not be comparable to the methodology used by other companies. Orders included in our backlog are represented by customer purchase orders and contracts, which we believe to be firm. Orders in the Process Control Systems business segment backlog at September 30, 2010, totaled \$36.9 million compared to \$36.2 million at September 30, 2009. We anticipate that approximately \$16.3 million of our ending fiscal 2010 backlog will be fulfilled during our 2011 fiscal year. Conditions outside of our control have caused us to experience some customer delays and cancellations of certain projects in the past; accordingly, backlog may not be indicative of future operating results as orders in our backlog may be cancelled or modified by our customers.

Employees

The Process Control Systems business segment had 125 full-time employees at September 30, 2010, primarily located in the United States. Our employees are not represented by unions, and we believe that our relationship with our employees is good.

Research and Development

The majority of research and development activities of this business segment are directed toward the development of our software suites for the management and control of the critical processes and facilities of our customers. Non-project research and development expenditures were \$0.4 million, \$0.3 million and \$0.3 million in fiscal years 2010, 2009 and 2008, respectively, and are reported in selling, general and administrative expenses in the Consolidated Statements of Operations.

Intellectual Property

While we are the holder of various copyrights related to software for this business segment, we do not consider any individual intellectual property to be material to our consolidated business operations.

Item 1A. *Risk Factors*

Our business is subject to a variety of risks and uncertainties, including, but not limited to, the most significant risks and uncertainties described below. Additional risks and uncertainties not known to us or not described below may also impair our business operations. If any of the following risks actually occur, our business, financial condition and results of operations could be harmed and we may not be able to achieve our goals. This Annual Report also includes statements reflecting assumptions, expectations, projections, intentions or beliefs about future events that are intended as forward-looking statements under the Private Securities Litigation Reform Act of 1995 and should be read in conjunction with the discussion under Forward-Looking Statements, above.

The ongoing economic uncertainty and financial market conditions have negatively impacted and may continue to impact our customer base, suppliers and backlog.

The ongoing economic downturn has reduced our backlog of orders. Various factors drive demand for our products and services, including the price of oil, capital expenditures, economic forecasts and financial markets. Continued uncertainty in the price of oil, capital expenditures, economic recovery or the financial markets could continue to impact our customers and severely impact the demand for projects that would result in orders for our products and services. If one or more of our suppliers or subcontractors experiences difficulties that result in a reduction or interruption in supply to us, or they fail to meet our manufacturing requirements, our business could be

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adversely impacted until we are able to secure alternative sources. Furthermore, our ability to expand our business would be limited in the future if we are unable to increase our bonding capacity or our credit facility on favorable terms or at all. These disruptions could lead to a lower demand for our products and services and could materially impact our business, financial condition and results of operations and potentially impact the trading price of our common stock.

Our operations could be adversely impacted by the Macondo well incident, the continuing effects from the U.S. government moratorium on offshore deepwater drilling projects and related new regulations.

On April 22, 2010, the drilling rig *Deepwater Horizon*, which was engaged in deepwater drilling operations in the U.S. Gulf of Mexico, sank after an explosion and fire. The incident resulted in a significant and uncontrolled oil spill off the coast of Louisiana. On May 28, 2010, the U.S. government imposed a six-month moratorium on all offshore deepwater drilling projects. A preliminary injunction was issued blocking enforcement of the moratorium on June 22, 2010, and the U.S. government issued a new moratorium on deepwater drilling on July 12, 2010. On October 12, 2010, the U.S. government lifted the moratorium. The U.S. government has also implemented additional safety and certification requirements applicable to drilling activities in the U.S. Gulf of Mexico, has imposed additional requirements with respect to development and production activities in the U.S. Gulf of Mexico and has delayed the approval of applications to drill in both deepwater and shallow-water areas. In addition, the U.S. government has announced that it intends to require that operators demonstrate their compliance with new regulations before resuming deepwater drilling. We cannot predict when, if at all, operators in the U.S. Gulf of Mexico will be able to satisfy these requirements. At this time, we cannot predict what, if any, impact the Macondo well incident, the continuing effects from the U.S. government moratorium on offshore deepwater drilling projects and related new regulations may have on the regulation of offshore oil and gas exploration and development activity, or what actions may be taken by our customers or other industry participants in response to the incident. Changes in laws or regulations regarding offshore oil and gas exploration and development activities and decisions by customers and other industry participants could reduce demand for our services, which would have a negative impact on our operations.

Our industry is highly competitive.

Many of our competitors are significantly larger and have substantially greater resources than we do. Competition in the industry depends on a number of factors, including price. Certain of our competitors may have lower cost structures and may, therefore, be able to provide their products or services at lower prices than we are able to provide. We cannot be certain that our competitors will not develop the expertise, experience and resources to provide products or services that are superior in both price and quality to our services. Similarly, we cannot be certain that we will be able to maintain or enhance our competitive position within our industry, maintain our customer base at current levels or increase our customer base.

International and political events may adversely affect our operations.

International sales accounted for approximately 29% of our revenues in fiscal 2010, including sales from our operations in the United Kingdom and Canada. We primarily operate in developed countries with historically stable operating and fiscal environments. Our consolidated results of operations, cash flows and financial condition could be adversely affected by the occurrence of political and economic instability; social unrest, acts of terrorism, force majeure, war or other armed conflict; inflation; currency fluctuations, devaluations and conversion restrictions; governmental activities that limit or disrupt markets, restrict payments or limit the movement of funds and trade restrictions and economic embargoes imposed by the United States or other countries.

Fluctuations in the price and supply of raw materials used to manufacture our products may reduce our profits.

Our raw material costs represented approximately 45% of our revenues for the fiscal year ended September 30, 2010. We purchase a wide variety of raw materials to manufacture our products, including steel, aluminum, copper and various electrical components. Unanticipated increases in raw material requirements or price increases could increase production costs and adversely affect profitability.

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Our volume of fixed-price contracts and use of percentage-of-completion accounting could result in volatility in our results of operations.

As discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations, Critical Accounting Policies and Estimates, and in Notes to Consolidated Financial Statements, a significant portion of our revenues is recognized on the percentage-of-completion method of accounting. The percentage-of-completion accounting practice we use results in our recognizing contract revenues and earnings ratably over the contract term in proportion to our incurrence of contract costs. The earnings or losses recognized on individual contracts are based on estimates of contract revenues, costs and profitability. The process of estimating costs on projects requires a significant amount of judgment and combines professional engineering, cost estimating, pricing and accounting inputs. Contract losses are recognized in full when determined, and contract profit estimates of revenue and cost to complete are adjusted based on ongoing reviews of estimated contract profitability. Previously recorded estimates are adjusted as the project progresses. In certain circumstances, it is possible that such adjustments could have a significant impact on our operating results for any fiscal quarter or year. Some of our contracts contain penalty provisions that require us to pay liquidated damages if we are responsible for the failure to meet specified contractual milestones and the applicable customer asserts a claim under these provisions. These contractual provisions define the conditions under which our customers may make claims against us to pay liquidated damages. In many cases in which we have had potential exposure for liquidated damages, such damages ultimately were not fully asserted by our customers.

Our acquisition strategy involves a number of risks.

Our strategy has been to pursue growth and product diversification through the acquisition of companies or assets that will enable us to expand our product and service offerings. We routinely review potential acquisitions. We may be unable to implement this strategy if we cannot reach agreement on potential strategic acquisitions on acceptable terms or for other reasons. Our acquisition strategy involves certain risks, including difficulties in the integration of operations and systems; failure to realize cost savings; the termination of relationships by key personnel and customers of the acquired company and a failure to add additional employees to handle the increased volume of business. Additionally, financial and accounting challenges and complexities in areas such as valuation, tax planning, treasury management and financial reporting from our acquisitions pose risks to our strategy. Due diligence may not reveal all risks and challenges associated with our acquisitions. A disruption of our ongoing business or an inability of our ongoing business to receive sufficient management attention could adversely affect profitability.

Financing for acquisitions may require us to obtain additional equity or debt financing, which, if available, may not be available on attractive terms.

Our backlog is subject to unexpected adjustments and cancellations and, therefore, may not be a reliable indicator of our future earnings.

We have a backlog of work to be completed on contracts. Orders included in our backlog are represented by customer purchase orders and contracts, which we believe to be firm. Backlog develops as a result of new business taken, which represents the revenue value of new project commitments received by us during a given period. Backlog consists of projects which either (1) have not yet been started or (2) are in progress and are not yet completed. In the latter case, the revenue value reported in backlog is the remaining value associated with work that has not yet been completed. From time to time, projects are canceled that appeared to have a high certainty of going forward at the time they were recorded as new business taken. In the event of a project cancellation, we may be reimbursed for certain costs but typically have no contractual right to the total revenue reflected in our backlog. In addition to our being unable to recover certain direct costs, canceled projects may also result in additional unrecoverable costs due to the resulting underutilization of our assets.

Our operating results may vary significantly from quarter to quarter.

Our quarterly results may be materially and adversely affected by changes in estimated costs or revenues under fixed-price contracts; the timing and volume of work under new agreements; general economic conditions; the

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spending patterns of customers; variations in the margins of projects performed during any particular quarter; losses experienced in our operations not otherwise covered by insurance; a change in the demand or production of our products and our services caused by severe weather conditions; a change in the mix of our customers, contracts and business; increases in design and manufacturing costs; the ability of customers to pay their invoices owed to us and disagreements with customers related to project performance on delivery.

Accordingly, our operating results in any particular quarter may not be indicative of the results that you can expect for any other quarter or for an entire year.

We may be unsuccessful at generating profitable internal growth.

Our ability to generate profitable internal growth will be affected by, among other factors, potential regulatory changes, our ability to attract new customers, increase the number or size of projects performed for existing customers, hire and retain employees and increase volume utilizing our existing facilities.

In addition, our customers may reduce the number or size of projects available to us. Many of the factors affecting our ability to generate internal growth may be beyond our control, and we cannot be certain that our strategies will be successful or that we will be able to generate cash flow sufficient to fund our operations and to support internal growth. If we are unsuccessful, we may not be able to achieve internal growth, expand our operations or grow our business.

The departure of key personnel could disrupt our business.

We depend on the continued efforts of our executive officers and senior management. We cannot be certain that any individual will continue in such capacity for any particular period of time. The loss of key personnel, or the inability to hire and retain qualified employees, could negatively impact our ability to manage our business.

Our business requires skilled labor, and we may be unable to attract and retain qualified employees.

Our ability to maintain our productivity and profitability will be limited by our ability to employ, train and retain skilled personnel necessary to meet our requirements. We may experience shortages of qualified personnel. We cannot be certain that we will be able to maintain an adequate skilled labor force necessary to operate efficiently and to support our growth strategy or that our labor expenses will not increase as a result of a shortage in the supply of skilled personnel. Labor shortages or increased labor costs could impair our ability to maintain our business or grow our revenues, and may adversely impact our profitability.

Actual and potential claims, lawsuits and proceedings could ultimately reduce our profitability and liquidity and weaken our financial condition.

We could be named as a defendant in future legal proceedings claiming damages from us in connection with the operation of our business. Most of the actions against us arise out of the normal course of our performing services or manufacturing equipment. We are and will likely continue to be a plaintiff in legal proceedings against customers, in which we seek to recover payment of contractual amounts due to us, as well as claims for increased costs incurred by us. When appropriate, we establish provisions against certain legal exposures, and we adjust such provisions from time to time according to ongoing developments related to each exposure. If in the future our assumptions and estimates related to such exposures prove to be inadequate or wrong, our consolidated results of operations, cash flows and financial condition could be adversely affected. In addition, claims, lawsuits and proceedings may harm our reputation or divert management resources away from operating our business.

We carry insurance against many potential liabilities, and our management of risk may leave us exposed to unidentified or unanticipated risks.

Although we maintain insurance policies with respect to our related exposures, including certain self-insured medical and dental programs, these policies contain deductibles, self-insured retentions and limits of coverage. We estimate our liabilities for known claims and unpaid claims and expenses based on information available as well as projections for claims incurred but not reported. However, insurance liabilities, some of which are self-insured, are

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difficult to estimate due to various factors. If any of our insurance policies or programs are not effective in mitigating our risks, we may incur losses that are not covered by our insurance policies or that exceed our accruals or that exceed our coverage limits and could adversely impact our consolidated results of operations, cash flows and financial position.

We may incur additional healthcare costs arising from federal healthcare reform legislation.

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 were signed into law in the U.S. This legislation expands health care coverage to many uninsured individuals and expands coverage to those already insured. The changes required by this legislation could cause us to incur additional healthcare and other costs, but we do not expect any material short-term impact on our financial results as a result of the legislation and are currently assessing the extent of any long-term impact.

Technological innovations by competitors may make existing products and production methods obsolete.

All of the products manufactured and sold by the Company depend upon the best available technology for success in the marketplace. The competitive environment is highly sensitive to technological innovation in both segments of our business. It is possible for competitors (both domestic and foreign) to develop products or production methods, which will make current products or methods obsolete or at least hasten their obsolescence.

Catastrophic events could disrupt our business.

The occurrence of catastrophic events ranging from natural disasters such as hurricanes to epidemics such as health epidemics to acts of war and terrorism could disrupt or delay the Company's ability to complete projects for its customers and could potentially expose the Company to third-party liability claims. Such events may or may not be fully covered by our various insurance policies or may be subject to deductibles. In addition, such events could impact the Company's customers and suppliers, resulting in temporary or long-term delays and/or cancellations of orders or raw materials used in normal business operations. These situations are outside the Company's control and could have a significant adverse impact on the results of operations.

Item 1B. *Unresolved Staff Comments*

None.

Item 2. *Properties*

We own or lease manufacturing facilities, sales offices, field offices and repair centers located throughout the United States and Canada, and we have a manufacturing facility located in the United Kingdom. Our facilities are generally located in areas that are readily accessible to raw materials and labor pools and are maintained in good condition. These facilities, together with recent expansions, are expected to meet our needs for the foreseeable future.

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Our principal locations by segment as of September 30, 2010, are as follows:

| Location | Number of Facilities | Acres | Approximate Square Footage | |
|-----------------------------------|-------------------------------------|--------------|---------------------------------------|---------------|
| | | | Owned | Leased |
| Electrical Power Products: | | | | |
| Houston, TX | 3 | 78.1 | 430,600 | 138,600 |
| North Canton, OH | 1 | 8.0 | 115,200 | |
| Northlake, IL | 1 | 10.0 | 103,500 | |
| Bradford, United Kingdom | 1 | 7.9 | 129,200 | |
| Edmonton, Alberta, Canada | 2 | | | 70,700 |
| Calgary, Alberta, Canada | 1 | | | 8,200 |
| Process Control Systems: | | | | |
| Pleasanton, CA | 1 | | | 21,200 |
| Duluth, GA | 1 | | | 29,700 |
| Chantilly, VA | 1 | | | 5,200 |
| East Rutherford, NJ | 1 | | | 8,700 |

All leased properties are subject to long-term leases with remaining lease terms ranging from one to 13 years as of September 30, 2010. We do not anticipate experiencing significant difficulty in retaining occupancy of any of our leased facilities through lease renewals prior to expiration or through month-to-month occupancy, or in replacing them with equivalent facilities.

Item 3. Legal Proceedings

We are involved in various legal proceedings, claims and other disputes arising in the ordinary course of business which, in general, are subject to uncertainties and the outcomes are not predictable. We do not believe that the ultimate conclusion of these disputes could materially affect our financial position or results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

We did not submit any matter to a vote of our stockholders during the fourth quarter of fiscal year 2010.

Table of Contents**PART II****Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*****Price Range of Common Stock**

Our common stock trades on the NASDAQ Global Market (NASDAQ) under the symbol POWL. The following table sets forth, for the periods indicated, the high and low sales prices per share as reported on the NASDAQ for our common stock.

| | High | Low |
|--------------------------|-------------|------------|
| Fiscal Year 2009: | | |
| First Quarter | \$ 41.00 | \$ 16.74 |
| Second Quarter | 37.31 | 23.25 |
| Third Quarter | 44.93 | 30.60 |
| Fourth Quarter | 42.55 | 33.73 |
| Fiscal Year 2010: | | |
| First Quarter | \$ 41.66 | \$ 30.32 |
| Second Quarter | 34.27 | 27.71 |
| Third Quarter | 36.10 | 27.01 |
| Fourth Quarter | 36.67 | 26.26 |

As of December 3, 2010, the last reported sales price of our common stock on the NASDAQ was \$36.97 per share. As of December 3, 2010, there were 536 stockholders of record of our common stock. All common stock held in street names are recorded in the Company's stock register as being held by one stockholder.

See Part III, Item 12 for information regarding securities authorized for issuance under our equity compensation plans.

Dividend Policy

Our current credit agreements limit the payment of dividends, other than dividends payable solely in our capital stock, without prior consent of our lenders. To date, we have not paid cash dividends on our common stock, and for the foreseeable future we intend to retain earnings for the development of our business. Future decisions to pay cash dividends will be at the discretion of the Board of Directors and will depend upon our results of operations, financial condition and capital expenditure plans and restrictive covenants under our credit facilities, along with other relevant factors.

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Performance Graph

The following Performance Graph and related information shall not be deemed soliciting material or to be filed with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Act of 1934, each as amended, except to the extent that we specifically incorporate it by reference into such filing.

The following graph compares, for the period from October 31, 2005, to September 30, 2010, the cumulative stockholder return on our common stock with the cumulative total return on the NASDAQ Market Index and Industrial Electrical Equipment Group (a select group of peer companies Advanced Energy Industries, Inc.; Altra Holdings Inc.; AZZ Inc.; CTC Corporation; DXP Enterprises Inc.; ENGlobal Corporation; ESCO Technologies Inc.; Franklin Electric Company, Inc.; Integrated Electrical Services, Inc.; Methode Electronics Inc. and Power-One Inc.). The comparison assumes that \$100 was invested on October 31, 2005, in our common stock, the NASDAQ Market Index and Industrial Electrical Equipment Group. The stock price performance reflected on the following graph is not necessarily indicative of future stock price performance.

**COMPARISON OF 5-YEAR CUMULATIVE TOTAL RETURN
AMONG POWELL INDUSTRIES, INC.,
INDUSTRIAL ELECTRICAL EQUIPMENT GROUP AND NASDAQ MARKET INDEX**

Item 6. Selected Financial Data

The selected financial data shown below for the past five years (including the 11-month period ended September 30, 2006) was derived from our audited financial statements. The historical results are not necessarily indicative of the operating results to be expected in the future. The selected financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and related notes included elsewhere in this Annual Report.

On December 15, 2009, we acquired Powell Canada. Powell Canada is headquartered in Edmonton, Alberta, Canada and provides electrical and maintenance services in western Canada. Powell Canada is also a manufacturer of switchgear and related products, primarily serving the oil and gas industry in western Canada. The operating results of Powell Canada, are included in our Electrical Power Products business segment from the acquisition date.

On August 7, 2006, we purchased certain assets related to the ANSI medium-voltage switchgear and circuit breaker business of GE's Consumer & Industrial unit. The operating results of the Power/Vac® product line are included from that date.

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On July 14, 2006, we acquired certain assets and hired the service and administrative employees of an electrical services company in Louisiana. The operating results of this acquisition are included in our Electrical Power Products business segment from that date.

| | 2010 | Years Ended September 30, | | | 11 Months Ended September 30, |
|--|--|--------------------------------------|-------------|-------------|--|
| | | 2009 | 2008 | 2007 | 2006 |
| | (In thousands, except per share data) | | | | |
| Statements of Operations: | | | | | |
| Revenues | \$ 550,692 | \$ 665,851 | \$ 638,704 | \$ 564,282 | \$ 374,547 |
| Cost of goods sold | 408,635 | 520,802 | 512,298 | 468,691 | 305,489 |
| Gross profit | 142,057 | 145,049 | 126,406 | 95,591 | 69,058 |
| Selling, general and administrative expenses | 84,457 | 79,954 | 80,416 | 73,639 | 54,172 |
| Amortization of intangible assets | 4,477 | 3,460 | 3,585 | 3,607 | 1,173 |
| Impairment of goodwill | 7,452 | | | | |
| Operating income | 45,671 | 61,635 | 42,405 | 18,345 | 13,713 |
| Interest expense, net | 610 | 976 | 2,537 | 2,943 | 698 |
| Income before income taxes | 45,061 | 60,659 | 39,868 | 15,402 | 13,015 |
| Income tax provision | 19,894 | 20,734 | 14,072 | 5,468 | 4,609 |
| Net income | 25,167 | 39,925 | 25,796 | 9,934 | 8,406 |
| Net (income) loss attributable to noncontrolling interest | (159) | (208) | 51 | (21) | 3 |
| Net income attributable to Powell Industries, Inc. | \$ 25,008 | \$ 39,717 | \$ 25,847 | \$ 9,913 | \$ 8,409 |
| Basic earnings per share attributable to Powell Industries, Inc. | \$ 2.17 | \$ 3.48 | \$ 2.29 | \$ 0.90 | \$ 0.77 |
| Diluted earnings per share attributable to Powell Industries, Inc. | \$ 2.14 | \$ 3.43 | \$ 2.26 | \$ 0.88 | \$ 0.76 |

| | 2010 | As of September 30, | | | 2006 |
|------------------------------------|-----------------------|----------------------------|-------------|-------------|-------------|
| | | 2009 | 2008 | 2007 | |
| | (In thousands) | | | | |
| Balance Sheet Data: | | | | | |
| Cash and cash equivalents | \$ 115,353 | \$ 97,403 | \$ 10,134 | \$ 5,257 | \$ 10,495 |
| Property, plant and equipment, net | 63,676 | 61,036 | 61,546 | 67,401 | 60,336 |

| | | | | | |
|--|---------|---------|---------|---------|---------|
| Total assets | 400,712 | 404,840 | 397,634 | 341,015 | 292,678 |
| Long-term debt and capital lease obligations, including current maturities | 6,885 | 9,492 | 41,758 | 35,836 | 42,396 |
| Total stockholders equity | 277,303 | 246,761 | 206,874 | 173,549 | 156,931 |
| Total liabilities and stockholders equity | 400,712 | 404,840 | 397,634 | 341,015 | 292,678 |

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

The following discussion should be read in conjunction with the accompanying consolidated financial statements and related notes. Any forward-looking statements made by or on our behalf are made pursuant to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995. Readers are cautioned that such forward-looking statements involve risks and uncertainties in that the actual results may differ materially from those projected in the forward-looking statements. For a description of the risks and uncertainties, please see [Cautionary](#)

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Statement Regarding Forward-Looking Statements; Risk Factors and Item 1A. Risk Factors contained in this Annual Report.

Overview

We develop, design, manufacture and service custom engineered-to-order equipment and systems for the management and control of electrical energy and other critical processes. Headquartered in Houston, Texas, we serve the transportation, environmental, energy, industrial and utility industries. Our business operations are consolidated into two business segments: Electrical Power Products and Process Control Systems. Revenues and costs are primarily related to engineered-to-order equipment and systems, which precludes us from providing detailed price and volume information.

Throughout fiscal years 2007 and 2008, we experienced strong market demand for our products and services. New investments in oil and gas infrastructure, as well as new investments by municipal and transit authorities to expand and improve public transportation, were key drivers of increased business volume with favorable margins in fiscal year 2009. Customer inquiries and requests for proposals remained strong throughout fiscal 2008 and the first half of fiscal 2009. Accordingly, we entered fiscal 2009 with a strong backlog of orders which resulted in record revenues in fiscal year 2009. Throughout the second half of 2009, customer inquiries and requests for proposal activity decreased and an increasing number of our customers began to cancel or delay the start of new capital projects for various reasons. This decreased our backlog of orders during 2009, and we began fiscal year 2010 with a backlog of \$365.8 million, a \$152.8 million decrease from the backlog of orders at the beginning of fiscal year 2009. The order backlog at September 30, 2010, was \$282.3 million. This decline in orders related to large capital projects with favorable margins in the second half of fiscal 2009 and throughout fiscal year 2010 will reduce our revenues and gross profits in fiscal year 2011, as compared to fiscal years 2009 and 2010.

On December 15, 2009, we acquired the business and certain assets of PowerComm Inc. and its subsidiaries, Redhill Systems Ltd., Nextron Corporation, PCG Technical Services Inc. and Concorde Metal Manufacturing Ltd (the entire business of which is referred to herein as Powell Canada). Powell Canada is headquartered in Edmonton, Alberta, Canada, and provides electrical and maintenance services in western Canada. Powell Canada is also a manufacturer of switchgear and related products, primarily serving the oil and gas industry in western Canada. The operating results of Powell Canada are included in our Electrical Power Products business segment from the acquisition date. In conjunction with the acquisition of Powell Canada, on April 1, 2010, we finalized the acquisition of a 50% ownership in a joint venture in Kazakhstan. The Company has made a strategic decision to exit this joint venture. For further information on the Powell Canada acquisition, see Note D of Notes to Consolidated Financial Statements.

Results of Operations

Twelve Months Ended September 30, 2010 (Fiscal 2010) Compared to Twelve Months Ended September 30, 2009 (Fiscal 2009)

Revenue and Gross Profit

Consolidated revenues decreased \$115.2 million to \$550.7 million in Fiscal 2010 compared to \$665.9 million in Fiscal 2009. Revenues decreased as a result of the decrease in demand for our products and services as discussed above. Domestic revenues decreased by 23.8% to \$393.3 million in Fiscal 2010 compared to \$516.0 million in Fiscal 2009. International revenues increased from \$149.9 million in Fiscal 2009 to \$157.6 million in Fiscal 2010. The acquisition of Powell Canada contributed approximately \$51.1 million of our international revenues during Fiscal 2010. Gross profit in Fiscal 2010 decreased by approximately \$3.0 million compared to Fiscal 2009, primarily as a result of lower revenues.

Consolidated gross profit, as a percentage of revenues, was 25.8% in Fiscal 2010 compared to 21.8% in Fiscal 2009. This increase in gross profit as a percentage of revenues resulted from strong market demand when the projects were negotiated, reduced costs on project completion from operational efficiencies, a reduced work force, reduced warranty costs, cancellation fees for orders that were cancelled from our backlog and the successful

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negotiation of change orders and the favorable negotiation of a customer claim for which the costs were previously recognized.

Electrical Power Products

Our Electrical Power Products business segment recorded revenues of \$524.2 million in Fiscal 2010, compared to \$637.9 million in Fiscal 2009. In Fiscal 2010, revenues from public and private utilities were approximately \$148.6 million compared to \$154.3 million in Fiscal 2009. The acquisition of Powell Canada contributed approximately \$51.1 million of revenue during Fiscal 2010. Revenues from commercial and industrial customers totaled \$338.0 million in Fiscal 2010, a decrease of \$94.5 million compared to Fiscal 2009. Municipal and transit projects generated revenues of \$37.6 million in Fiscal 2010 compared to \$51.1 million in Fiscal 2009.

Business segment gross profit, as a percentage of revenues, was 25.5% in Fiscal 2010 compared to 20.9% in Fiscal 2009. This increase in gross profit as a percentage of revenues resulted from strong market demand when the projects were negotiated, reduced costs on project completion from operational efficiencies, a reduced workforce, reduced warranty costs, cancellation fees for orders that were cancelled from our backlog and the successful negotiation of change orders and the favorable negotiation of a customer claim for which the costs were previously recognized.

Process Control Systems

In Fiscal 2010, our Process Control Systems business segment recorded revenues of \$26.5 million, a decrease from \$28.0 million in Fiscal 2009. Business segment gross profit, as a percentage of revenues, decreased to 31.3% for Fiscal 2010, compared to 40.8% for Fiscal 2009. This decrease in revenues and gross profit as a percentage of revenues is related to the mix of jobs currently in the backlog and revenues of \$3.5 million and gross profit of \$2.8 million in the third quarter of Fiscal 2009, resulting from a mediated settlement related to a previously completed contract that was in dispute for several years.

For additional information related to our business segments, see Note N of Notes to Consolidated Financial Statements.

Consolidated Selling, General and Administrative Expenses

Consolidated selling, general and administrative expenses increased to 15.3% of revenues in Fiscal 2010 compared to 12.0% of revenues in Fiscal 2009. Selling, general and administrative expenses increased to \$84.5 million in Fiscal 2010 compared to \$80.0 million in Fiscal 2009. This increase was primarily related to the acquisition of Powell Canada and includes acquisition-related costs of approximately \$2.4 million. Selling, general and administration expenses increased as a percentage of revenues as a result of our decline in revenues, along with the fact that portions of our sales and administrative support infrastructure is necessary to support our customers, invest in information systems, continue research and development and pursue project opportunities.

Amortization of Intangible Assets

Amortization of intangible assets increased to \$4.5 million in Fiscal 2010, compared to \$3.5 million in Fiscal 2009. This increase was from the amortization of the intangible assets recorded as a result of the acquisition of Powell Canada.

Impairment of Goodwill

An impairment of goodwill of approximately \$7.5 million was recorded in Fiscal 2010 related to the Powell Canada acquisition. The Company's strategic decision to exit the 50% owned joint venture in Kazakhstan and delays in the anticipated growth in capital investments in the Oil Sands Region of western Canada, relative to our expectations, resulted in the impairment charge.

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Interest Income and Expense

Interest expense was \$0.9 million in Fiscal 2010, a decrease of approximately \$0.2 million compared to Fiscal 2009. The decrease in interest expense was primarily due to lower amounts outstanding under our U.S. and U.K. credit facilities during Fiscal 2010.

Interest income was \$0.3 million in Fiscal 2010 compared to \$0.1 million in Fiscal 2009. This increase resulted from larger cash amounts being invested during Fiscal 2010.

Income Tax Provision

Our provision for income taxes reflects an effective tax rate on earnings before income taxes of 44.1% in Fiscal 2010 compared to 34.2% in Fiscal 2009. The increase in the effective tax rate was primarily related to the valuation allowance recorded related to foreign deferred tax assets.

Net Income Attributable to Powell Industries, Inc.

In Fiscal 2010, we recorded net income of \$25.0 million, or \$2.14 per diluted share, compared to \$39.7 million, or \$3.43 per diluted share, in Fiscal 2009. We generated improved gross profits as a percentage of revenues for the Company as a whole as a result of favorable margins on project completion due to operational efficiencies and cancellation fees for orders that were cancelled from our backlog, along with the successful negotiation of change orders and the favorable negotiation of a customer claim in Fiscal 2010 for which costs were previously recognized. Net income for Fiscal 2010 was negatively impacted by the impairment of goodwill of approximately \$7.5 million and the valuation allowance recorded on foreign deferred tax assets of approximately \$3.7 million. As previously discussed, net income in Fiscal 2009 included the benefit of the \$3.5 million mediated settlement, reduced by legal and other expenses of approximately \$0.7 million, net of tax, related to a previously completed contract that was in dispute for several years.

Backlog

The order backlog at September 30, 2010, was \$282.3 million, compared to \$365.8 million at September 30, 2009. New orders placed during Fiscal 2010 totaled \$466.8 million compared to \$511.2 million in Fiscal 2009. Backlog decreased during the second half of Fiscal 2009 and into Fiscal 2010 due to the ongoing economic downturn which has led our customers to reduce and delay spending on new capital projects. This decline in backlog throughout Fiscal 2010 negatively impacted our revenues in Fiscal 2010 and will continue to negatively impact our revenues going into 2011.

Fiscal 2009 Compared to Twelve Months Ended September 30, 2008 (Fiscal 2008)

Revenue and Gross Profit

Consolidated revenues increased \$27.2 million to \$665.9 million in Fiscal 2009 compared to \$638.7 million in Fiscal 2008. Revenues increased as we responded to strong market demand by increasing our capacity and throughput. Domestic revenues increased by 10.0% to \$516.0 million in Fiscal 2009 compared to \$469.1 million in Fiscal 2008. International revenues decreased from \$169.6 million in Fiscal 2008 to \$149.9 million in Fiscal 2009, primarily as the result of changes in the British Pound Sterling-to-U.S. Dollar exchange rate. The increase in consolidated revenues was primarily due to an increased sales effort and strong market demand in Fiscal 2008 and the first half of Fiscal 2009. Gross profit in Fiscal 2009 increased by approximately \$18.6 million compared to Fiscal 2008 as a result of our ability to absorb our fixed costs and improved pricing as a result of strong market activity.

Electrical Power Products

Our Electrical Power Products business segment recorded revenues of \$637.9 million in Fiscal 2009, compared to \$611.5 million in Fiscal 2008. In Fiscal 2009, revenues from public and private utilities were approximately \$154.3 million compared to \$171.8 million in Fiscal 2008. Revenues from commercial and industrial customers

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totaled \$432.5 million in Fiscal 2009, an increase of \$32.5 million compared to Fiscal 2008. Municipal and transit projects generated revenues of \$51.1 million in Fiscal 2009 compared to \$39.7 million in Fiscal 2008.

Business segment gross profit, as a percentage of revenues, was 20.9% in Fiscal 2009 compared to 19.3% in Fiscal 2008. The increase in gross profit as a percentage of revenues was attributable to efficiencies resulting from an increase in production volume and improved pricing as a result of strong market activity.

Process Control Systems

In Fiscal 2009, our Process Control Systems business segment recorded revenues of \$28.0 million, up from \$27.2 million in Fiscal 2008. Business segment gross profit increased as a percentage of revenues, to 40.8% for Fiscal 2009, compared to 30.2% for Fiscal 2008. This increase resulted from a favorable mix of jobs and increased efficiencies through regionalization of operations. Revenues and gross profit benefited in Fiscal 2009 by approximately \$3.5 million and \$2.8 million, respectively, due to a mediated settlement related to a previously completed contract that was in dispute for several years.

For additional information related to our business segments, see Note N of Notes to Consolidated Financial Statements.

Consolidated Selling, General and Administrative Expenses

Consolidated selling, general and administrative expenses decreased to 12.0% of revenues in Fiscal 2009 compared to 12.6% of revenues in Fiscal 2008. Selling, general and administrative expenses decreased to \$80.0 million in Fiscal 2009 compared to \$80.4 million in Fiscal 2008. This decrease was primarily a result of decreased commissions and incentive compensation. Selling, general and administrative expenses as a percentage of revenues decreased primarily due to our ability to leverage our existing infrastructure to support our increased production volume, along with the timing of commissions related to new orders.

Interest Income and Expense

Interest expense was \$1.1 million in Fiscal 2009, a decrease of approximately \$1.8 million compared to Fiscal 2008. The decrease in interest expense was primarily due to lower interest rates and the lower amounts outstanding under our credit facility during Fiscal 2009.

Interest income was \$0.1 million in Fiscal 2009 compared to \$0.4 million in Fiscal 2008. This decrease resulted from lower interest rates being earned on amounts invested.

Income Tax Provision

Our provision for income taxes reflects an effective tax rate on earnings before income taxes of 34.2% in Fiscal 2009 compared to 35.3% in Fiscal 2008. The decrease in the effective tax rate resulted primarily from an agreement reached with the taxing authorities in the United Kingdom resulting in a reduction in tax expense of approximately \$568,000 related to foreign tax credits from previous years.

Net Income Attributable to Powell Industries, Inc.

In Fiscal 2009, we recorded net income of \$39.7 million, or \$3.43 per diluted share, compared to \$25.8 million, or \$2.26 per diluted share, in Fiscal 2008. We generated higher revenues and improved gross profits for the Company as a whole, while leveraging our existing infrastructure to support our increased production volume. As previously

discussed, net income in Fiscal 2009 included the benefit of the \$3.5 million mediated settlement, reduced by legal and other expenses of approximately \$0.7 million, net of tax, related to a previously completed contract that was in dispute for several years.

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Backlog

The order backlog at September 30, 2009, was \$365.8 million, compared to \$518.6 million at September 30, 2008. New orders placed during Fiscal 2009 totaled \$511.2 million compared to \$705.4 million in Fiscal 2008. Our decline in backlog was due to the amount of projects completed being greater than the amount of orders received.

Liquidity and Capital Resources

Cash and cash equivalents increased to approximately \$115.4 million at September 30, 2010, as a result of cash flow provided by operations of approximately \$64.1 million for Fiscal 2010. The approximately \$64.1 million of cash flow from operations resulted from net income and our continued efforts to manage inventory and billings to customers. As of September 30, 2010, current assets exceeded current liabilities by 2.6 times and our debt to total capitalization ratio was 2.4%.

At September 30, 2010, we had cash and cash equivalents of \$115.4 million, compared to \$97.4 million at September 30, 2009. We have a \$58.5 million revolving credit facility in the U.S. and an additional £4.0 million (approximately \$6.3 million) revolving credit facility in the United Kingdom, both of which expire in December 2012. As of September 30, 2010, there were no amounts borrowed under these lines of credit. We also have a \$19.4 million revolving credit facility and a \$2.4 million single advance term loan in Canada. At September 30, 2010, there was no balance outstanding under the Canadian revolving credit facility or the Canadian term loan. Total long-term debt and capital lease obligations, including current maturities, totaled \$6.9 million at September 30, 2010, compared to \$9.5 million at September 30, 2009. Letters of credit outstanding were \$15.2 million and \$17.6 million at September 30, 2010 and 2009, respectively, which reduce our availability under our credit facilities. Amounts available under the U.S. revolving credit facility and the revolving credit facility in the United Kingdom were approximately \$43.3 million and \$6.3 million, respectively, at September 30, 2010. Amounts available under the Canadian revolving credit facility were approximately \$14.4 million at September 30, 2010. For further information regarding our debt, see Notes H and L of Notes to Consolidated Financial Statements.

Operating Activities

During Fiscal 2010, cash provided by operating activities was approximately \$64.1 million. Cash flow from operations is primarily influenced by demand for our products and services and is impacted as our progress payment terms with our customers are matched with the payment terms with our suppliers. During Fiscal 2009, cash provided by operating activities was approximately \$127.0 million. The increase in Fiscal 2009 cash flow from operations resulted primarily from net income and our increased efforts to manage inventory and billings to customers. During Fiscal 2008, cash used in operating activities was approximately \$5.2 million. Cash flow from operations was negatively impacted as accounts receivable and inventories increased due to higher volume as a result of demand for our products and services.

Investing Activities

Investments in property, plant and equipment during Fiscal 2010 totaled approximately \$4.4 million compared to \$8.1 million and \$3.4 million in Fiscal 2009 and 2008, respectively. During Fiscal 2010, we acquired Powell Canada for approximately \$23.4 million. Additionally, approximately \$0.6 million was paid to acquire the noncontrolling interest related to our joint venture in Singapore (Powell Asia), which has been strategically realigned from an operating entity to a sales and marketing function within Powell. Our capital expenditures in Fiscal 2009 related primarily to the expansion of one of our operating facilities and for upgrades to our enterprise resource planning system (ERP system).

There were no material proceeds from the sale of fixed assets in Fiscal 2010, 2009 or 2008. Proceeds from the sale of fixed assets in Fiscal 2009 were primarily from the sale of idled manufacturing facilities and equipment.

Financing Activities

Net cash used in financing activities was approximately \$19.4 million in Fiscal 2010, as we paid down our Canadian revolving line of credit and term loan from the cash flow provided by our operating activities. Net cash

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used in financing activities was approximately \$30.4 million in Fiscal 2009 because we paid down our U.S. and U.K. revolving lines of credit and the term loan from the cash flow provided by our operating activities. Net cash provided by financing activities was approximately \$13.8 million in Fiscal 2008. The primary source of cash in financing activities in Fiscal 2008 was due to borrowings on the U.S. revolving line of credit and proceeds from the exercise of stock options, which were used to fund operations and capital expenditures.

Contractual and Other Obligations

At September 30, 2010, our long-term contractual obligations were limited to debt and leases. The table below details our commitments by type of obligation, including interest if applicable, and the period that the payment will become due (in thousands).

| As of September 30, 2010, Payments Due by Period: | Long-Term Debt Obligations | Capital Lease Obligations | Operating Lease Obligations | Total |
|--|---|--|--|--------------|
| Less than 1 year | \$ 424 | \$ 1,403 | \$ 3,362 | \$ 5,189 |
| 1 to 3 years | 842 | 830 | 5,002 | 6,674 |
| 3 to 5 years | 833 | 23 | 729 | 1,585 |
| More than 5 years | 2,846 | | 1 | 2,847 |
| Total long-term contractual obligations | \$ 4,945 | \$ 2,256 | \$ 9,094 | \$ 16,295 |

As of September 30, 2010, the total unrecognized tax benefit related to uncertain tax positions was approximately \$0.8 million. We estimate that none of this will be paid within the next 12 months. However, we believe that it is reasonably possible that within the next 12 months unrecognized tax benefits will remain unchanged due to the expiration of certain statutes of limitations. We are unable to make reasonably reliable estimates regarding the timing of future cash outflows, if any, associated with the remaining unrecognized tax benefits.

Other Commercial Commitments

We are contingently liable for secured and unsecured letters of credit of \$18.2 million as of September 30, 2010, of which \$15.2 million reduces our borrowing capacity.

The following table reflects potential cash outflows that may result from a contingent event related to our letters of credit (in thousands):

| As of September 30, 2010, Payments Due by Period: | Letters of Credit |
|--|------------------------------|
| Less than 1 year | \$ 10,042 |
| 1 to 3 years | 7,857 |
| 3 to 5 years | 135 |
| More than 5 years | 156 |
| Total long-term commercial obligations | \$ 18,190 |

We also had performance and maintenance bonds totaling approximately \$185.3 million that were outstanding at September 30, 2010. Performance and maintenance bonds are used to guarantee contract performance to our customers.

Outlook

We participate in large capital-intensive projects in the oil and gas, petrochemical, utility and transportation markets, which can take several years to plan and execute. Once our customers begin the construction phase, projects are typically completed. Our record revenues in Fiscal 2009 were driven by the large number and size of capital projects that were planned and initiated over the previous two years.

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However, our backlog of orders going into our fiscal year 2011 (Fiscal 2011) is approximately \$282.3 million, a decrease of \$83.5 million from the beginning backlog of orders going into Fiscal 2010. Throughout the second half of Fiscal 2009 and continuing into Fiscal 2010, customer inquiries and requests for proposal activity decreased and an increasing number of our customers cancelled or delayed the start of new capital projects. We believe these delays resulted from the short-term reduction in the demand for oil, uncertainty in the worldwide economy and financial markets, as well as increasing uncertainty as to the impact that potential regulatory changes could have on their business.

Growth in demand for energy is expected to continue over the long term. New infrastructure investments will be needed to ensure the available supply of petroleum products. New power generation and distribution infrastructure will also be needed to meet the growing demand for electrical energy. New power generation plants will also be needed to replace the aging facilities across the United States, as those plants reach the end of their life cycle. A heightened concern for environmental damage, together with the uncertainty of gasoline prices, has expanded the popularity of urban transit systems and pushed ridership to an all-time high, which will drive new investment in transit infrastructure. Opportunities for future projects continue; however, the timing of many of these projects is difficult to predict. The demand for our products and services will increase as investments in large capital-intensive infrastructure projects begins to receive funding and support.

We believe that cash available and borrowing capacity under our existing credit facilities should be sufficient to finance anticipated operational activities, capital improvements and debt repayments for the foreseeable future. During this period of continued economic and market uncertainty, we will continue to monitor the factors that drive our markets. We will strive to maintain our leadership and competitive advantage in the markets we serve while aligning our cost structures with market conditions.

Effects of Inflation

We have experienced price volatility related to raw materials, primarily copper, aluminum and steel, during the past three years. Fixed-price contracts can limit our ability to pass cost increases to our customers, thus negatively impacting our earnings. We anticipate that the volatility in commodity prices could impact our operations in Fiscal 2011.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosures of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates. We believe the following accounting policies and estimates to be critical in the preparation and reporting of our consolidated financial statements.

Revenue Recognition

Our revenues are primarily generated from engineering and manufacturing of custom products under long-term contracts that may last from one month to several years, depending on the contract. Revenues from long-term contracts are recognized on the percentage-of-completion method of accounting.

Under the percentage-of-completion method of accounting, revenues are recognized as work is performed primarily based on the estimated completion to date calculated by multiplying the total contract price by percentage of performance to date, based on total costs or total labor dollars incurred to date to the total estimated costs or total labor

dollars estimated at completion. The method used to determine the percentage of completion is typically the cost method, unless the labor method is a more accurate method of measuring the progress of the project. Application of the percentage-of-completion method of accounting requires the use of estimates of costs to be incurred for the performance of the contract. Contract costs include all direct material, direct labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and all costs associated with operation of equipment. The cost estimation process is based upon the professional knowledge and experience of the Company's engineers, project managers and financial professionals. Factors that are considered in estimating

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the work to be completed and ultimate contract recovery include the availability and productivity of labor, the nature and complexity of the work to be performed, the effect of change orders, the availability of materials, the effect of any delays in our project performance and the recoverability of any claims. Changes in job performance, job conditions, estimated profitability and final contract settlements, including our estimate of liquidated damages, if any, may result in revisions to costs and income, with their effects being recognized in the period in which the revisions are determined. Whenever revisions of estimated contract costs and contract values indicate that the contract costs will exceed estimated revenues, thus creating a loss, a provision for the total estimated loss is recorded in that period.

Revenues associated with maintenance, repair and service contracts are recognized when the services are performed. Expenses related to these types of services are recognized as incurred.

Allowance for Doubtful Accounts

We maintain and continually assess the adequacy of an allowance for doubtful accounts representing our estimate for losses resulting from the inability of our customers to pay amounts due to us. This estimated allowance is based on historical experience of uncollected accounts, the level of past due accounts, the overall level of outstanding accounts receivable, information about specific customers with respect to their inability to make payments and expectations of future conditions that could impact the collectibility of accounts receivable. However, future changes in our customers operating performance and cash flows, or in general economic conditions, could have an impact on their ability to fully pay these amounts, which, among other things, could have a material adverse impact on our operating results.

Impairment of Long-Lived Assets

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be realizable. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if an impairment of such asset is necessary. This requires us to make long-term forecasts of the future revenues and costs related to the assets subject to review. Forecasts require assumptions about demand for our products and future market conditions. Estimating future cash flows requires significant judgment, and our projections may vary from cash flows eventually realized. Future events and unanticipated changes to assumptions could require a provision for impairment in a future period. The effect of any impairment would be reflected in income (loss) from operations in the Consolidated Statements of Operations. In addition, we estimate the useful lives of our long-lived assets and other intangibles and periodically review these estimates to determine whether these lives are appropriate.

Intangible Assets

Goodwill and other intangible assets with indefinite useful lives are no longer amortized, but are evaluated for impairment annually, or immediately if conditions indicate that impairment could exist. The evaluation requires a two-step impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss. The first step of the test compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of the impairment loss. Both steps of the goodwill impairment testing involve significant estimates.

The costs of intangible assets with determinable useful lives are amortized over their estimated useful lives. When certain events or changes in operating conditions occur, an impairment assessment is performed and lives of intangible assets with determinable lives may be adjusted.

See Note E of the Notes to Consolidated Financial Statements for a discussion of our impairment recorded related to the goodwill associated with the acquisition of Powell Canada and the 50% ownership in the operations in a joint venture in Kazakhstan.

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Accruals for Contingent Liabilities

From time to time, contingencies such as insurance and legal claims arise in the normal course of business. Pursuant to current accounting standards, we must evaluate such contingencies to subjectively determine the likelihood that an asset has been impaired or a liability has been incurred at the date of the financial statements, as well as evaluating whether the amount of the loss can be reasonably estimated. If the likelihood is determined to be probable and it can be reasonably estimated, the estimated loss is recorded. The amounts we record for insurance claims, warranties, legal and other contingent liabilities require judgments regarding the amount of expenses that will ultimately be incurred. We use past experience and history, as well as the specific circumstances surrounding each contingent liability, in evaluating the amount of liability that should be recorded. Actual results could differ from our estimates.

Warranty Costs

We provide for estimated warranty costs at the time of sale based upon historical rates applicable to individual product lines. In addition, specific provisions are made when the costs of such warranties are expected to exceed accruals. We use past experience and historical claims to determine the estimated liability. Actual results could differ from our estimate.

Accounting for Income Taxes

We account for income taxes under the asset and liability method, based on the income tax laws and rates in the countries in which operations are conducted and income is earned. This approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax basis of assets and liabilities. Developing our provision for income taxes requires significant judgment and expertise in federal, international and state income tax laws, regulations and strategies, including the determination of deferred tax assets and liabilities and, if necessary, any valuation allowances that may be required for deferred tax assets. We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. We believe that the deferred tax asset recorded as of September 30, 2010, is realizable through future reversals of existing taxable temporary differences and future taxable income. If we were to subsequently determine that we would be able to realize deferred tax assets in the future in excess of our net recorded amount, an adjustment to deferred tax assets would increase earnings for the period in which such determination was made. We will continue to assess the adequacy of the valuation allowance on a quarterly basis. Our judgments and tax strategies are subject to audit by various taxing authorities.

The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. We recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Accounting literature also provides guidance on derecognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, and income tax disclosures. Judgment is required in assessing the future tax consequences of events that have been recognized in our financial statements or tax returns. Variations in the actual outcome of these future tax consequences could materially impact our financial statements.

See Note I of the Notes to Consolidated Financial Statements for disclosures related to the valuation allowance recorded related to foreign deferred tax assets.

Foreign Currency Translation

The functional currency for our foreign subsidiaries is the local currency in which the entity is located. The financial statements of all subsidiaries with a functional currency other than the U.S. Dollar have been translated into U.S. Dollars. All assets and liabilities of foreign operations are translated into U.S. Dollars using year-end exchange rates, and all revenues and expenses are translated at average rates during the respective period. The

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U.S. Dollar results that arise from such translation, as well as exchange gains and losses on intercompany balances of a long-term investment nature, are included in the cumulative currency translation adjustments in accumulated other comprehensive income in stockholders' equity.

Derivative Financial Instruments

As part of managing our exposure to changes in foreign currency exchange rates, we periodically utilize foreign exchange forward contracts. The objective of these contracts is to minimize impacts to cash flows and profitability due to changes in foreign currency exchange rates on accounts receivable, accounts payable and forecasted cash transactions. These contracts are recorded in the consolidated balance sheets at fair value, which is based upon an income approach consisting of a discounted cash flow model that takes into account the present value of the future cash flows under the terms of the contracts using current market information, such as foreign currency spot and forward rates, as of the reporting date.

We formally document our hedging relationships, including identifying the hedging instruments and the hedged items, as well as our risk management objectives and strategies for undertaking the hedge transactions. We also formally assess, both at inception and at least quarterly thereafter, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the cash flows of the hedged item. The effective portion of the change in fair value of a derivative is recorded as a component of accumulated other comprehensive income in the consolidated balance sheets. When the hedged item affects the consolidated statement of operations, the gain or loss included in accumulated other comprehensive income is reported on the same line in the consolidated statements of operations as the hedged item. In addition, any ineffective portion of the changes in the fair value of derivatives used as cash flow hedges is reported in the consolidated statements of operations as the changes occur. If it is determined that a derivative ceases to be a highly effective hedge, or it is probable that the forecasted transaction will not occur, we discontinue hedge accounting and any unrealized gains or losses are recorded in the consolidated statement of operations.

On January 1, 2009, we adopted accounting guidance that amended and expanded the disclosure requirements related to derivative instruments and hedging activities. This guidance enhances the disclosure requirements for derivative instruments and hedging activities. The guidance is focused on requiring enhanced disclosure on: 1) how and why an entity uses derivative instruments and hedging activities; 2) how derivative instruments and related hedging activities are accounted for and 3) how derivative instruments and related hedging activities affect an entity's cash flows, financial position and performance.

To accomplish the three objectives listed above, we are required to provide: 1) qualitative disclosures regarding the objectives and strategies for using derivative instruments and engaging in hedging activities in the context of our overall risk exposure; 2) quantitative disclosure in tabular format of the fair values of derivative instruments and their gains and losses and 3) disclosures about credit-risk related contingent features in derivative instruments.

New Accounting Pronouncements

In December 2007, the FASB issued accounting guidance on business combinations. The guidance establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. The accounting guidance also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. The guidance is effective as of the beginning of an entity's fiscal year that begins after December 15, 2008, and was adopted by us on October 1, 2009. Refer to Note D for additional information regarding our recent acquisition of Powell Canada and the impact of this guidance.

In December 2007, the FASB issued accounting guidance for noncontrolling interests in consolidated financial statements. This guidance establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The accounting guidance also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. The guidance is effective as of the beginning of an entity's fiscal year that begins after December 15, 2008,

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and was adopted by us on October 1, 2009. This guidance did not have an impact on our consolidated financial position or results of operations, but did change the presentation of noncontrolling interests in our Consolidated Balance Sheets and Consolidated Statements of Operations.

In December 2008, the FASB issued accounting guidance on employers' disclosures about postretirement benefit plan assets. The disclosures about plan assets required by this guidance shall be provided for fiscal years beginning after December 15, 2009, and will be adopted by us in the first quarter of fiscal year 2011. We do not expect adoption of this guidance to have a material impact on our consolidated financial statements.

In April 2009, the FASB issued accounting guidance regarding the accounting for assets acquired and liabilities assumed in a business combination due to contingencies. This guidance clarifies the initial and subsequent recognition, subsequent accounting and disclosure of assets and liabilities arising from contingencies in a business combination. This guidance requires that assets acquired and liabilities assumed in a business combination that arise from contingencies be recognized at fair value, if the acquisition-date fair value can be reasonably estimated. If the acquisition-date fair value of an asset or liability cannot be reasonably estimated, the asset or liability would be measured at the amount that would be recognized using the accounting guidance related to accounting for contingencies or the guidance for reasonably estimating losses. This accounting guidance became effective for us on October 1, 2010. The adoption of this guidance did not have a material impact on our consolidated financial statements.

In January 2010, the FASB issued updated guidance to amend the disclosure requirements related to recurring and nonrecurring fair value measurements. This update requires new disclosures about significant transfers of assets and liabilities between Level 1 and Level 2 of the fair value hierarchy (including the reasons for these transfers) and the reasons for any transfers in or out of Level 3. This update also requires a reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements on a gross basis. In addition to these new disclosure requirements, this update clarifies certain existing disclosure requirements. For example, this update clarifies that reporting entities are required to provide fair value measurement disclosures for each class of assets and liabilities, rather than each major category of assets or liabilities. This update also clarifies the requirement for entities to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. This update will become effective for us with the interim and annual reporting period beginning after December 15, 2009, our fiscal year 2011, except for the requirement to provide the Level 3 activity of purchases, sales, issuances and settlements on a gross basis, which will become effective for us with the interim and annual reporting period beginning after December 15, 2010, our fiscal year 2012. We will not be required to provide the amended disclosures for any previous periods presented for comparative purposes. Other than requiring additional disclosures, adoption of this update will not have a material impact on our consolidated financial statements.

In April 2010, the FASB issued accounting guidance for the milestone method of revenue recognition. This guidance allows entities to make a policy election to use the milestone method of revenue recognition and provides guidance on defining a milestone and the criteria that should be met for applying the milestone method. The scope of this guidance is limited to transactions involving milestones relating to research and development deliverables. The guidance includes enhanced disclosure requirements about each arrangement, individual milestones and related contingent consideration, information about substantive milestones and factors considered in the determination. This guidance is effective prospectively to milestones achieved in fiscal years, and interim periods within those years, beginning after June 15, 2010. Early application and retrospective application are permitted. We have evaluated this new guidance and have determined that it will not currently have a significant impact on the determination or reporting of our financial results.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

We are exposed to certain market risks arising from transactions we have entered into in the normal course of business. These risks primarily relate to fluctuations in interest rates, foreign exchange rates and commodity prices.

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Interest Rate Risk

We are subject to market risk resulting from changes in interest rates related to our floating rate bank credit facility. At September 30, 2010, \$15.2 million was outstanding, bearing interest at approximately 2.5% per year. A hypothetical 100 basis point increase in variable interest rates would result in a total annual increase in interest expense of approximately \$152,000. While we do not currently have any derivative contracts to hedge our exposure to interest rate risk, we have in the past and may in the future enter into such contracts. During each of the past three years, we have not experienced a significant effect on our business due to changes in interest rates.

Foreign Currency Transaction Risk

We have operations that expose us to currency risk in the British Pound Sterling, the Canadian Dollar and to a lesser extent the Euro. Amounts invested in our foreign operations are translated into U.S. Dollars at the exchange rates in effect at the balance sheet date. The resulting translation adjustments are recorded as accumulated other comprehensive income (loss), a component of stockholders' equity in our consolidated balance sheets. We believe the exposure to the effects that fluctuating foreign currencies have on our consolidated results of operations is limited because the foreign operations primarily invoice customers and collect obligations in their respective currencies or U.S. Dollars. Our international operations are financed utilizing local credit facilities denominated in local currencies. Additionally, expenses associated with these transactions are generally contracted and paid for in the same local currencies. A 10% unfavorable change in the U.S. Dollar exchange rate, relative to other functional currencies in which we operate, would not materially impact our consolidated balance sheet at September 30, 2010.

During Fiscal 2009 and Fiscal 2010, we entered into eight foreign currency forward contracts to manage the volatility of future cash flows on certain long-term contracts that are denominated in the British Pound Sterling. The contracts are designated as cash flow hedges for accounting purposes. The changes in fair value related to the effective portion of the hedges are recognized as a component of accumulated other comprehensive income on our consolidated balance sheets. At September 30, 2010, we recorded a net liability of approximately \$47,000 on our consolidated balance sheets related to these transactions.

Commodity Price Risk

We are subject to market risk from fluctuating market prices of certain raw materials. While such materials are typically available from numerous suppliers, commodity raw materials are subject to price fluctuations. We attempt to pass along such commodity price increases to our customers on a contract-by-contract basis to avoid a negative effect on profit margin. While we may do so in the future, we have not currently entered into any derivative contracts to hedge our exposure to commodity risk. We continue to experience price volatility with some of our key raw materials and components. Fixed-price contracts may limit our ability to pass cost increases to our customers, thus negatively impacting our earnings. Fluctuations in commodity prices may have a material impact on our future earnings and cash flows.

Market Risk

We are also exposed to general market and other risk and its potential impact on accounts receivable or costs and estimated earnings in excess of billings on uncompleted contracts. The amounts recorded may be at risk if our customers' ability to pay these obligations is negatively impacted by economic conditions. Our customers and their industries are typically EPC firms, oil and gas producers, oil and gas pipelines, refineries, petrochemical plants, electrical power generators, public and private utilities, co-generation facilities, mining/metals operations, pulp and paper plants, transportation authorities, governmental agencies and other large industrial customers. We maintain ongoing discussions with customers regarding contract status with respect to payment status, change orders and billing

terms in an effort to monitor collections of amounts billed.

Item 8. *Financial Statements and Supplementary Data*

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| Financial Statements: | |
| <u>Report of Independent Registered Public Accounting Firm</u> | 30 |
| <u>Consolidated Balance Sheets as of September 30, 2010 and 2009</u> | 31 |
| <u>Consolidated Statements of Operations for the Years Ended September 30, 2010, 2009 and 2008</u> | 32 |
| <u>Consolidated Statements of Stockholders' Equity for the Years Ended September 30, 2010, 2009 and 2008</u> | 33 |
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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
and Stockholders of Powell Industries, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Powell Industries, Inc. and its subsidiaries at September 30, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2010 in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2010, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management’s Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company’s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As described in Management’s Report on Internal Control over Financial Reporting appearing under Item 9A, management has excluded Powell Canada from its assessment of internal control over financial reporting as of September 30, 2010 because it was acquired by the Company in a purchase business combination in December 2009.

We have also excluded Powell Canada from our audit of internal control over financial reporting. Powell Canada is a wholly-owned subsidiary whose total assets and total revenues represent 10% and 9%, respectively, of the related consolidated financial statement amounts as of and for the year ended September 30, 2010.

/s/ PricewaterhouseCoopers LLP

Houston, Texas
December 8, 2010

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**
(In thousands, except share and per share data)

| | September 30, | |
|--|----------------------|-------------------|
| | 2010 | 2009 |
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 115,353 | \$ 97,403 |
| Accounts receivable, less allowance for doubtful accounts of \$907 and \$1,607, respectively | 91,766 | 114,274 |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 38,064 | 46,335 |
| Inventories, net | 38,244 | 46,252 |
| Income taxes receivable | 6,726 | 695 |
| Deferred income taxes | 3,087 | 3,303 |
| Prepaid expenses and other current assets | 8,951 | 6,741 |
| Total Current Assets | 302,191 | 315,003 |
| Property, plant and equipment, net | 63,676 | 61,036 |
| Goodwill | 1,003 | 1,084 |
| Intangible assets, net | 26,132 | 21,305 |
| Other assets | 7,710 | 6,412 |
| Total Assets | \$ 400,712 | \$ 404,840 |

LIABILITIES AND STOCKHOLDERS EQUITY

| | | |
|---|----------------|----------------|
| Current Liabilities: | | |
| Current maturities of long-term debt and capital lease obligations | \$ 1,683 | \$ 4,692 |
| Income taxes payable | 1,500 | 7,637 |
| Accounts payable | 41,850 | 48,124 |
| Accrued salaries, bonuses and commissions | 25,064 | 24,503 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 31,009 | 44,772 |
| Accrued product warranty | 5,929 | 7,558 |
| Other accrued expenses | 7,711 | 11,856 |
| Total Current Liabilities | 114,746 | 149,142 |
| Long-term debt and capital lease obligations, net of current maturities | 5,202 | 4,800 |
| Deferred compensation | 2,730 | 2,685 |
| Postretirement benefit obligation | 532 | 784 |
| Other liabilities | 199 | 212 |
| Total Liabilities | 123,409 | 157,623 |

Commitments and Contingencies (Note L)

Equity:

Stockholders' Equity:

| | | |
|--|------------|------------|
| Preferred stock, par value \$.01; 5,000,000 shares authorized; none issued | | |
| Common stock, par value \$.01; 30,000,000 shares authorized; 11,676,955 and 11,479,610 shares issued, respectively; 11,676,955 and 11,479,610 shares outstanding, respectively | 117 | 115 |
| Additional paid-in capital | 34,546 | 29,970 |
| Retained earnings | 244,969 | 219,961 |
| Accumulated other comprehensive income (loss) | (1,352) | (2,716) |
| Deferred compensation | (977) | (569) |
| | | |
| Total Stockholders' Equity | 277,303 | 246,761 |
| Noncontrolling interest | | 456 |
| | | |
| Total Equity | 277,303 | 247,217 |
| | | |
| Total Liabilities and Equity | \$ 400,712 | \$ 404,840 |

The accompanying notes are an integral part of these consolidated financial statements.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

| | Year Ended September 30, | | |
|---|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| Revenues | \$ 550,692 | \$ 665,851 | \$ 638,704 |
| Cost of goods sold | 408,635 | 520,802 | 512,298 |
| Gross profit | 142,057 | 145,049 | 126,406 |
| Selling, general and administrative expenses | 84,457 | 79,954 | 80,416 |
| Amortization of intangible assets | 4,477 | 3,460 | 3,585 |
| Impairment of goodwill | 7,452 | | |
| Operating income | 45,671 | 61,635 | 42,405 |
| Interest expense | 870 | 1,107 | 2,892 |
| Interest income | (260) | (131) | (355) |
| Income before income taxes | 45,061 | 60,659 | 39,868 |
| Income tax provision | 19,894 | 20,734 | 14,072 |
| Net income | 25,167 | 39,925 | 25,796 |
| Net (income) loss attributable to noncontrolling interest | (159) | (208) | 51 |
| Net income attributable to Powell Industries, Inc. | \$ 25,008 | \$ 39,717 | \$ 25,847 |
| Earnings per share attributable to Powell Industries, Inc.: | | | |
| Basic | \$ 2.17 | \$ 3.48 | \$ 2.29 |
| Diluted | \$ 2.14 | \$ 3.43 | \$ 2.26 |
| Weighted average shares: | | | |
| Basic | 11,545 | 11,424 | 11,265 |
| Diluted | 11,693 | 11,591 | 11,452 |

The accompanying notes are an integral part of these consolidated financial statements.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
(In thousands)

| | Other Compre- hensive Income | Common Shares | Stock Amount | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income/(Loss) | Deferred Compensation | Total |
|--|---------------------------------------|------------------|-----------------|----------------------------------|----------------------|--|--------------------------|------------|
| Balance, September 30, 2007 | | 11,144 | \$ 111 | \$ 16,854 | \$ 154,572 | \$ 2,557 | \$ (545) | \$ 173,549 |
| Net income | \$ 25,847 | | | | 25,847 | | | 25,847 |
| Foreign currency translation adjustments | (2,395) | | | | | (2,395) | | (2,395) |
| Amortization of deferred compensation-ESOP | | | | | | | 387 | 387 |
| Exercise of stock options | | 239 | 3 | 4,234 | | | | 4,237 |
| Stock-based compensation | | | | 2,166 | | | | 2,166 |
| Income tax benefit from stock options exercised | | | | 2,510 | | | | 2,510 |
| Amortization of restricted stock | | | | 290 | | | 134 | 424 |
| Deferred compensation restricted stock | | 7 | | 111 | | | | 111 |
| Issuance of restricted stock | | 14 | | 716 | | | (716) | |
| Adjustment from adoption of accounting guidance on the accounting for uncertainty in income taxes | | | | 40 | (175) | | | (135) |
| Postretirement benefit adjustment, net of tax of \$97 | 173 | | | | | 173 | | 173 |
| Total comprehensive income | 23,625 | | | | 25,847 | (2,222) | | 23,625 |
| Balance, September 30, 2008 | | 11,404 | 114 | 26,921 | 180,244 | 335 | (740) | 206,874 |
| Net income | 39,717 | | | | 39,717 | | | 39,717 |
| Foreign currency translation adjustments | (2,867) | | | | | (2,867) | | (2,867) |
| Amortization of deferred compensation-ESOP | | | | | | | 158 | 158 |
| Exercise of stock options | | 31 | 1 | 513 | | | | 514 |
| Stock-based compensation | | 29 | | 1,623 | | | | 1,623 |
| | | | | 291 | | | | 291 |

| | | | | | | | | |
|--|-----------|--------|--------|-----------|------------|------------|----------|------------|
| Income tax benefit from stock options exercised | | | | | | | 476 | 476 |
| Amortization of restricted stock | | | | | | | (463) | 159 |
| Issuance of restricted stock | 16 | | 622 | | | | | |
| Unrealized loss on cash flow hedges, net of tax of \$164 | (304) | | | | | (304) | | (304) |
| Postretirement benefit adjustment, net of tax of \$67 | 120 | | | | | 120 | | 120 |
| Total comprehensive income | 36,666 | | | 39,717 | | (3,051) | | 36,666 |
| Balance, September 30, 2009 | | 11,480 | 115 | 29,970 | 219,961 | (2,716) | (569) | 246,761 |
| Net income | 25,008 | | | | 25,008 | | | 25,008 |
| Foreign currency translation adjustments | 1,467 | | | | | 1,467 | | 1,467 |
| Exercise of stock options | | 109 | 1 | 1,699 | | | | 1,700 |
| Stock-based compensation | | 58 | 1 | 1,113 | | | (322) | 792 |
| Income tax benefit from stock options exercised | | | | 878 | | | | 878 |
| Amortization of restricted stock | | | | | | | 467 | 467 |
| Issuance of restricted stock | | 30 | | 886 | | | (553) | 333 |
| Unrealized loss on cash flow hedges, net of tax of \$265 | (206) | | | | | (206) | | (206) |
| Postretirement benefit adjustment, net of tax of \$58 | 103 | | | | | 103 | | 103 |
| Total comprehensive income | \$ 26,372 | | | | 25,008 | 1,364 | | 26,372 |
| Balance, September 30, 2010 | | 11,677 | \$ 117 | \$ 34,546 | \$ 244,969 | \$ (1,352) | \$ (977) | \$ 277,303 |

The accompanying notes are an integral part of these consolidated financial statements.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

| | Year Ended September 30, | | |
|---|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| Operating Activities: | | | |
| Net income | \$ 25,167 | \$ 39,925 | \$ 25,796 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | | |
| Depreciation | 9,154 | 7,493 | 8,133 |
| Amortization | 4,549 | 3,469 | 3,740 |
| Impairment of goodwill | 7,452 | | |
| Stock-based compensation | 1,929 | 2,256 | 2,592 |
| Bad debt expense | 410 | 959 | 637 |
| Deferred income taxes | (348) | (1,447) | 318 |
| Changes in operating assets and liabilities: | | | |
| Accounts receivable, net | 39,687 | 15,392 | (27,146) |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 8,243 | 35,701 | (14,062) |
| Inventories | 12,320 | 25,884 | (25,513) |
| Prepaid expenses and other current assets | (5,813) | (3,432) | 657 |
| Other assets | 440 | (194) | |
| Accounts payable and income taxes payable | (20,281) | (4,891) | (4,916) |
| Accrued liabilities | (5,392) | (40) | 10,422 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | (13,762) | 5,789 | 13,773 |
| Other | 378 | 120 | 381 |
| Net cash provided by (used in) operating activities | 64,133 | 126,984 | (5,188) |
| Investing Activities: | | | |
| Proceeds from sale of fixed assets | 14 | 30 | |
| Purchases of property, plant and equipment | (4,420) | (8,081) | (3,428) |
| Purchase of noncontrolling interest Powell Asia | (659) | | |
| Acquisition of Powell Canada | (23,394) | | |
| Net cash used in investing activities | (28,459) | (8,051) | (3,428) |
| Financing Activities: | | | |
| Borrowings on US revolving line of credit | | 50,953 | 229,480 |
| Payments on US revolving line of credit | | (69,953) | (212,480) |
| Payments on UK revolving line of credit | | (2,388) | (1,596) |
| Payments on UK term loan | | (4,223) | (2,343) |
| Borrowings on Canadian revolving line of credit | 891 | | |
| Payments on Canadian revolving line of credit | (13,984) | | |

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| | | | |
|--|------------|-----------|-----------|
| Payments on Canadian term loan | (2,429) | | |
| Payments on industrial development revenue bonds | (400) | (400) | (400) |
| Payments on deferred acquisition payable | (4,292) | (5,220) | (5,563) |
| Payments on short-term and other financing | (1,087) | (13) | (52) |
| Proceeds from exercise of stock options | 1,700 | 515 | 4,236 |
| Tax benefit from exercise of stock options | 209 | 291 | 2,510 |
| Net cash (used in) provided by financing activities | (19,392) | (30,438) | 13,792 |
| Net increase in cash and cash equivalents | 16,282 | 88,495 | 5,176 |
| Effect of exchange rate changes on cash and cash equivalents | 1,668 | (1,226) | (299) |
| Cash and cash equivalents at beginning of year | 97,403 | 10,134 | 5,257 |
| Cash and cash equivalents at end of year | \$ 115,353 | \$ 97,403 | \$ 10,134 |

The accompanying notes are an integral part of these consolidated financial statements.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. Business and Organization

Powell Industries, Inc. (we, us, our, Powell or the Company) was incorporated in the state of Delaware in 2004 as a successor to a Nevada company incorporated in 1968. The Nevada corporation was the successor to a company founded by William E. Powell in 1947, which merged into the Company in 1977. Our major subsidiaries, all of which are wholly-owned, include: Powell Electrical Systems, Inc.; Transdyn, Inc.; Powell Industries International, Inc.; Switchgear & Instrumentation Limited (S&I) and Powell Canada Inc.

We develop, design, manufacture and service custom engineered-to-order equipment and systems for the management and control of electrical energy and other critical processes. Headquartered in Houston, Texas, we serve the transportation, environmental, energy, industrial and utility industries.

On December 15, 2009, we acquired the business and certain assets of PowerComm Inc. and its subsidiaries, Redhill Systems Ltd., Nextron Corporation, PCG Technical Services Inc. and Concorde Metal Manufacturing Ltd (the entire business of which is referred to herein as Powell Canada) for \$23.4 million, not including expenses. Powell Canada is headquartered in Edmonton, Alberta, Canada, and provides electrical and maintenance services in western Canada. Powell Canada is also a manufacturer of switchgear and related products, primarily serving the oil and gas industry in western Canada. The operating results of Powell Canada are included in our Electrical Power Products business segment from the acquisition date. In conjunction with the acquisition of Powell Canada, on April 1, 2010, we finalized the acquisition of a 50% ownership in a joint venture in Kazakhstan. Our interest in the net assets of the 50% ownership in the joint venture is recorded at its estimated net realizable value, as the Company has made a strategic decision to exit this joint venture. For further information on the Powell Canada acquisition, see Note D.

B. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Powell and our wholly-owned subsidiaries. The financial position and results of operation of our Singapore joint venture, in which we held a majority ownership, have also been consolidated. As a result of this consolidation, we record noncontrolling interest on our balance sheet for our joint venture partner's share of equity in the joint venture. All significant intercompany accounts and transactions have been eliminated in consolidation.

Reclassifications

Certain reclassifications have been made in prior years' financial statements to conform to the presentation used in the current year. These reclassifications have not resulted in any changes to previously reported net income for any periods.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (U.S. GAAP) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying footnotes. The most significant estimates used in our financial statements affect revenue and cost recognition for construction contracts, the allowance for doubtful accounts,

goodwill, self-insurance, warranty accruals, income taxes, postretirement benefit obligations and estimates related to acquisition valuations. The amounts recorded for insurance claims, warranties, legal, income taxes and other contingent liabilities require judgments regarding the amount of expenses that will ultimately be incurred. We base our estimates on historical experience and on various other assumptions, as well as the specific circumstances surrounding these contingent liabilities, in evaluating the amount of liability that should be recorded. Estimates may change as new events occur, additional information becomes available or operating environments change. Actual results may differ from our estimates.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)*****Cash and Cash Equivalents***

Cash and cash equivalents include cash on hand, deposits with banks and highly liquid investments with original maturities of three months or less.

Supplemental Disclosures of Cash Flow Information (in thousands):

| | Year Ended September 30, | | |
|----------------------------------|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| Cash paid during the period for: | | | |
| Interest | \$ 563 | \$ 439 | \$ 1,447 |
| Income taxes, net of refunds | 31,993 | 21,527 | 3,641 |

Fair Value of Financial Instruments

Financial instruments include cash, short-term investments, marketable securities, receivables, payables and debt obligations. Except as described below, due to the short-term nature of the investments, the book value is representative of their fair value. The carrying value of debt approximates fair value as interest rates are indexed to the Federal Funds Rate, the London interbank offered rate (LIBOR) or the bank's prime rate.

The deferred acquisition payable was discounted based on a rate of approximately 6.6%, which approximated our incremental borrowing rate for obligations of a similar nature. The carrying value of this debt approximates fair value. For additional information regarding the deferred acquisition payable, see Note H.

Accounts Receivable

Accounts receivable are stated net of allowances for doubtful accounts. We maintain and continually assess the adequacy of the allowance for doubtful accounts representing our estimate for losses resulting from the inability of our customers to pay amounts due to us. This estimated allowance is based on historical experience of uncollected accounts, the level of past due accounts, the overall level of outstanding accounts receivable, information about specific customers with respect to their inability to make payments and expectations of future conditions that could impact the collectibility of accounts receivable. Future changes in our customers' operating performance and cash flows or in general economic conditions could have an impact on their ability to fully pay these amounts, which could have a material impact on our operating results. In most cases, receivables are not collateralized. However, we utilize letters of credit to secure payment on sales when possible. At September 30, 2010 and 2009, accounts receivable included retention amounts of \$9.0 million and \$8.1 million, respectively. Retention amounts are in accordance with applicable provisions of engineering and construction contracts and become due upon completion of contractual requirements. Approximately \$1.3 million of the retained amount at September 30, 2010, is expected to be collected subsequent to September 30, 2011.

Costs and Estimated Earnings in Excess of Billings on Uncompleted Contracts

Costs and estimated earnings in excess of billings on uncompleted contracts arise when revenues are recorded on a percentage-of-completion basis but cannot be invoiced under the terms of the contract. Such amounts are invoiced upon completion of contractual milestones.

Costs and estimated earnings in excess of billings on uncompleted contracts also include certain costs associated with unapproved change orders. These costs are included when change order approval is probable. Amounts are carried at the lower of cost or net realizable value. No profit is recognized on costs incurred until change order approval is obtained. The amounts recorded involve the use of judgments and estimates; thus, actual recoverable amounts could differ from original assumptions. See Note L – Commitments and Contingencies for a discussion related to certain costs recorded in costs and estimated earnings in excess of billings on uncompleted contracts.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In accordance with industry practice, assets and liabilities related to costs and estimated earnings in excess of billings on uncompleted contracts, as well as billings in excess of costs and estimated earnings on uncompleted contracts, have been classified as current. The contract cycle for certain long-term contracts may extend beyond one year; thus, collection of amounts related to these contracts may extend beyond one year.

Inventories

Inventories are stated at the lower of cost or market using first-in, first-out (FIFO) or weighted-average methods and include the cost of materials, labor and manufacturing overhead. We use estimates in determining the level of reserves required to state inventory at the lower of cost or market. Our estimates are based on market activity levels, production requirements, the physical condition of products and technological innovation. Changes in any of these factors may result in adjustments to the carrying value of inventory.

Property, Plant and Equipment

Property, plant and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets. Expenditures for repairs and maintenance are charged to expense when incurred. Expenditures for major renewals and improvements, which extend the useful lives of existing equipment, are capitalized and depreciated. Upon retirement or disposition of property, plant and equipment, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in the Consolidated Statements of Operations.

Impairment of Long-Lived Assets and Amortization of Intangible Assets

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be realizable. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if an impairment of such asset is necessary. This requires us to make long-term forecasts of the future revenues and the costs related to the assets subject to review. Forecasts require assumptions about demand for our products and future market conditions. Estimating future cash flows requires significant judgment, and our projections may vary from cash flows eventually realized. Future events and unanticipated changes to assumptions could require a provision for impairment in a future period. The effect of any impairment would be reflected in income (loss) from operations in the Consolidated Statements of Operations. In addition, we estimate the useful lives of our long-lived assets and other intangibles and periodically review these estimates to determine whether these lives are appropriate.

The costs of intangible assets with determinable useful lives are amortized over their estimated useful lives. When certain events or changes in operating conditions occur, an impairment assessment is performed and lives of intangible assets with determinable lives may be adjusted. For additional information regarding our intangible assets and related impairment, see Note E.

Goodwill and Indefinite Lived Assets

Goodwill and other intangible assets with indefinite useful lives are evaluated for impairment annually, or immediately if conditions indicate that impairment could exist. The evaluation requires a two-step impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss. The first step of the

test compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of the impairment loss. Both steps of the goodwill impairment testing involve significant estimates.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Income Taxes

We account for income taxes under the asset and liability method, based on the income tax laws and rates in the countries in which operations are conducted and income is earned. This approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax basis of assets and liabilities. Developing our provision for income taxes requires significant judgment and expertise in federal, international and state income tax laws, regulations and strategies, including the determination of deferred tax assets and liabilities and, if necessary, any valuation allowances that may be required for deferred tax assets. We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. We believe that the deferred tax asset recorded as of September 30, 2010, is realizable through future reversals of existing taxable temporary differences and future taxable income. If we were to subsequently determine that we would be able to realize deferred tax assets in the future in excess of our net recorded amount, an adjustment to deferred tax assets would increase earnings for the period in which such determination was made. We will continue to assess the adequacy of the valuation allowance on a quarterly basis. Our judgments and tax strategies are subject to audit by various taxing authorities.

The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. We recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Accounting literature also provides guidance on derecognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, and income tax disclosures. Judgment is required in assessing the future tax consequences of events that have been recognized in our financial statements or tax returns. Variations in the actual outcome of these future tax consequences could materially impact our financial statements.

Revenue Recognition

Our revenues are primarily generated from engineering and manufacturing of custom products under long-term contracts that may last from one month to several years, depending on the contract. Revenues from long-term contracts are recognized on the percentage-of-completion method of accounting.

Under the percentage-of-completion method of accounting, revenues are recognized as work is performed primarily based on the estimated completion to date calculated by multiplying the total contract price by percentage of performance to date, based on total costs or total labor dollars incurred to date to the total estimated costs or total labor dollars estimated at completion. The method used to determine the percentage of completion is typically the cost method, unless the labor method is a more accurate method of measuring the progress of the projects. Application of the percentage-of-completion method of accounting requires the use of estimates of costs to be incurred for the performance of the contract. Contract costs include all direct material, direct labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and all costs associated with operation of equipment. The cost estimation process is based upon the professional knowledge and experience of our engineers, project managers and financial professionals. Factors that are considered in estimating the work to be completed and ultimate contract recovery include the availability and productivity of labor, the nature and complexity of the work to

be performed, the effect of change orders, the availability of materials, the effect of any delays in our project performance and the recoverability of any claims. Changes in job performance, job conditions, estimated profitability and final contract settlements, including our estimate of liquidated damages, if any, may result in revisions to costs and income, with their effects being recognized in the period in which the revisions are determined. Whenever revisions of estimated contract costs and contract values indicate that the contract costs will exceed estimated revenues, thus creating a loss, a provision for the total estimated loss is recorded in that period.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Revenues associated with maintenance, repair and service contracts are recognized when the services are performed. Expenses related to these types of services are recognized as incurred.

Warranties

We provide for estimated warranty costs at the time of sale based upon historical rates applicable to individual product lines. In addition, specific provisions are made when the costs of such warranties are expected to exceed accruals. Our standard terms and conditions of sale include a warranty for parts and service for the earlier of 18 months from the date of shipment or 12 months from the date of initial operations.

Research and Development Expense

Research and development costs are charged to expense as incurred. These costs are included as a component of selling, general and administrative expenses on the Consolidated Statements of Operations. Such amounts were \$6.5 million, \$6.0 million and \$6.6 million in fiscal years 2010, 2009 and 2008, respectively.

Foreign Currency Translation

The functional currency for our foreign subsidiaries is the local currency in which the entity is located. The financial statements of all subsidiaries with a functional currency other than the U.S. Dollar have been translated into U.S. Dollars. All assets and liabilities of foreign operations are translated into U.S. Dollars using year-end exchange rates, and all revenues and expenses are translated at average rates during the respective period. The U.S. Dollar results that arise from such translation, as well as exchange gains and losses on intercompany balances of a long-term investment nature, are included in the cumulative currency translation adjustments in accumulated other comprehensive income in stockholders' equity.

Stock-Based Compensation

We measure stock-based compensation cost at the grant date based on the fair value of the award and recognize it as expense over the applicable vesting period of the stock award (generally five years) using the straight-line method. Excess income tax benefits related to share-based compensation expense that must be recognized directly in equity are considered financing rather than operating cash flow activities.

We use the Black-Scholes option pricing model, with expanded guidance for the development of our assumption used as inputs, to estimate the fair value of our stock options. Expected volatility is determined using volatilities based on historical stock prices for a period equal to the expected term. The expected volatility assumption is adjusted if future volatility is expected to vary from historical experience. The expected term of options represents the period of time that options granted are expected to be outstanding and falls between the options' vesting and contractual expiration dates. The risk-free interest rate is based on the yield at the date of grant of a zero-coupon U.S. Treasury bond whose maturity period equals the options' expected term. There have been no stock options granted since July 2005.

Derivative Financial Instruments

As part of managing our exposure to changes in foreign currency exchange rates, we periodically utilize foreign exchange forward contracts. The objective of these contracts is to minimize impacts to cash flows and profitability

due to changes in foreign currency exchange rates on accounts receivable, accounts payable and forecasted cash transactions. These contracts are recorded in the Consolidated Balance Sheets at fair value, which is based upon an income approach consisting of a discounted cash flow model that takes into account the present value of the future cash flows under the terms of the contracts using current market information as of the reporting date, such as foreign currency spot and forward rates.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We formally document our hedging relationships, including identifying the hedging instruments and the hedged items, as well as our risk management objectives and strategies for undertaking the hedge transaction. We also formally assess, both at inception and at least quarterly thereafter, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the cash flows of the hedged item. The effective portion of the change in fair value of a derivative is recorded as a component of accumulated other comprehensive income in the Consolidated Balance Sheets. When the hedged item affects the income statement, the gain or loss included in accumulated other comprehensive income is reported on the same line in the Consolidated Statements of Operations as the hedged item. In addition, any ineffective portion of the changes in the fair value of derivatives used as cash flow hedges is reported in the Consolidated Statements of Operations as the changes occur. If it is determined that a derivative ceases to be a highly effective hedge, or it is probable that the forecasted transaction will not occur, we discontinue hedge accounting and any unrealized gains or losses are recorded in the consolidated financial statements.

On January 1, 2009, we adopted accounting guidance that amended and expanded the disclosure requirements related to derivative instruments and hedging activities. This guidance enhances the disclosure requirements for derivative instruments and hedging activities. The guidance is focused on requiring enhanced disclosure on: 1) how and why an entity uses derivative instruments and hedging activities; 2) how derivative instruments and related hedging activities are accounted for and 3) how derivative instruments and related hedging activities affect an entity's cash flows, financial position and performance.

To accomplish the three objectives listed above, we are required to provide: 1) qualitative disclosures regarding the objectives and strategies for using derivative instruments and engaging in hedging activities in the context of our overall risk exposure; 2) quantitative disclosure in tabular format of the fair values of derivative instruments and their gains and losses and 3) disclosures about credit-risk related contingent features in derivative instruments.

The adoption of this accounting guidance did not have an impact on our consolidated financial position or results of operations. As a result of the adoption of this guidance, we have expanded our disclosures regarding derivative instruments and hedging activities within Note J.

Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss), which is included as a component of stockholders' equity net of tax, includes unrealized gains or losses on derivative instruments, postretirement benefit adjustments and currency translation adjustments in foreign consolidated subsidiaries.

Fair Value Measurements

On October 1, 2008, we adopted authoritative guidance issued by the Financial Accounting Standards Board (FASB) related to fair value measurements. The authoritative guidance defines fair value, establishes a framework for measuring fair value under U.S. GAAP and expands disclosures about fair value measurements. The authoritative guidance was effective for us beginning October 1, 2008, for financial assets and liabilities. Refer to Note C for additional information regarding our fair value measurements for financial assets and liabilities. The changes became effective for non-financial assets and liabilities recognized or disclosed at fair value on a nonrecurring basis beginning October 1, 2009. The application of the authoritative guidance, as it relates to non-financial assets and liabilities, had no impact on our consolidated financial statements.

New Accounting Standards

In December 2007, the FASB issued accounting guidance on business combinations. The guidance establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. The accounting guidance also establishes disclosure requirements to enable the evaluation of the nature and financial

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

effects of the business combination. The guidance is effective as of the beginning of an entity's fiscal year that begins after December 15, 2008, and was adopted by us on October 1, 2009. Refer to Note D for additional information regarding our recent acquisition of Powell Canada and the impact of this guidance.

In December 2007, the FASB issued accounting guidance for noncontrolling interests in consolidated financial statements. This guidance establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The accounting guidance also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. The guidance is effective as of the beginning of an entity's fiscal year that begins after December 15, 2008, and was adopted by us on October 1, 2009. This guidance did not have an impact on our consolidated financial position or results of operations, but did change the presentation of noncontrolling interests in our Consolidated Balance Sheets and Consolidated Statements of Operations.

In December 2008, the FASB issued accounting guidance on employers' disclosures about postretirement benefit plan assets. The disclosures about plan assets required by this guidance shall be provided for fiscal years beginning after December 15, 2009, and will be adopted by us in the first quarter of fiscal year 2011. We do not expect adoption of this guidance to have a material impact on our consolidated financial statements.

In April 2009, the FASB issued accounting guidance regarding the accounting for assets acquired and liabilities assumed in a business combination due to contingencies. This guidance clarifies the initial and subsequent recognition, subsequent accounting and disclosure of assets and liabilities arising from contingencies in a business combination. This guidance requires that assets acquired and liabilities assumed in a business combination that arise from contingencies be recognized at fair value, if the acquisition-date fair value can be reasonably estimated. If the acquisition-date fair value of an asset or liability cannot be reasonably estimated, the asset or liability would be measured at the amount that would be recognized using the accounting guidance related to accounting for contingencies or the guidance for reasonably estimating losses. This accounting guidance became effective for us on October 1, 2010. The adoption of this guidance did not have a material impact on our consolidated financial statements.

In January 2010, the FASB issued updated guidance to amend the disclosure requirements related to recurring and nonrecurring fair value measurements. This update requires new disclosures about significant transfers of assets and liabilities between Level 1 and Level 2 of the fair value hierarchy (including the reasons for these transfers) and the reasons for any transfers in or out of Level 3. This update also requires a reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements on a gross basis. In addition to these new disclosure requirements, this update clarifies certain existing disclosure requirements. For example, this update clarifies that reporting entities are required to provide fair value measurement disclosures for each class of assets and liabilities, rather than each major category of assets or liabilities. This update also clarifies the requirement for entities to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. This update will become effective for us with the interim and annual reporting period beginning after December 15, 2009, our fiscal year 2011, except for the requirement to provide the Level 3 activity of purchases, sales, issuances and settlements on a gross basis, which will become effective for us with the interim and annual reporting period beginning after December 15, 2010, our fiscal year 2012. We will not be required to provide the amended disclosures for any previous periods presented for comparative purposes. Other than requiring additional

disclosures, adoption of this update will not have a material impact on our consolidated financial statements.

In April 2010, the FASB issued accounting guidance for the milestone method of revenue recognition. This guidance allows entities to make a policy election to use the milestone method of revenue recognition and provides guidance on defining a milestone and the criteria that should be met for applying the milestone method. The scope of this guidance is limited to transactions involving milestones relating to research and development deliverables.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The guidance includes enhanced disclosure requirements about each arrangement, individual milestones and related contingent consideration, information about substantive milestones and factors considered in the determination. This guidance is effective prospectively to milestones achieved in fiscal years, and interim periods within those years, beginning after June 15, 2010. Early application and retrospective application are permitted. We have evaluated this new guidance and have determined that it will not currently have a significant impact on the determination or reporting of our financial results.

Subsequent Events

We evaluated subsequent events through the time of filing this Annual Report on Form 10-K. No significant events occurred subsequent to the balance sheet or prior to the filing of this report that would have a material impact on our consolidated financial statements or results of operations.

C. Fair Value Measurements

We measure certain financial assets and liabilities at fair value. Fair value is defined as an exit price which represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in valuing an asset or liability. The accounting guidance requires the use of valuation techniques to measure fair value that maximize the use of observable inputs and minimize the use of unobservable inputs. As a basis for considering such assumptions and inputs, a fair value hierarchy has been established which identifies and prioritizes three levels of inputs to be used in measuring fair value.

The three levels of the fair value hierarchy are as follows:

Level 1 Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Inputs other than the quoted prices in active markets that are observable either directly or indirectly, including: quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active or other inputs that are observable or can be corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market data and require the reporting entity to develop its own assumptions.

The following table summarizes the fair value of our assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2010 (in thousands):

| Fair Value Measurements at September 30, 2010 | | | |
|--|--|--------------------|--|
| Quoted Prices in Active Markets for | Significant Other Observable Inputs | Significant | Fair Value at September 30, |

| | Identical Assets (Level 1) | (Level 2) | Unobservable Inputs (Level 3) | 2010 |
|------------------------------------|---|------------------|--|-------------|
| <i>Assets</i> | | | | |
| Cash equivalents | \$ 64,014 | \$ | \$ | \$ 64,014 |
| Total | \$ 64,014 | \$ | \$ | \$ 64,014 |
| <i>Liabilities</i> | | | | |
| Foreign currency forward contracts | \$ | \$ 47 | \$ | \$ 47 |
| Total | \$ | \$ 47 | \$ | \$ 47 |

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table summarizes the fair value of our assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2009 (in thousands):

| | Fair Value Measurements at September 30, 2009 | | | Fair Value at September 30, 2009 |
|------------------------------------|---|--|--|---|
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | |
| Assets | | | | |
| Cash equivalents | \$ 59,324 | \$ | \$ | \$ 59,324 |
| Total | \$ 59,324 | \$ | \$ | \$ 59,324 |
| Liabilities | | | | |
| Foreign currency forward contracts | \$ | \$ 752 | \$ | \$ 752 |
| Total | \$ | \$ 752 | \$ | \$ 752 |

Cash equivalents, primarily funds held in money market savings instruments, are reported at their current carrying value which approximates fair value due to the short-term nature of these instruments and are included in cash and cash equivalents in our Consolidated Balance Sheets.

Foreign currency forward contracts are valued using an income approach which consists of a discounted cash flow model that takes into account the present value of future cash flows under the terms of the contracts using observable market spot and forward rates as of our reporting date, and are included in Level 2 inputs in the above tables. We use these derivative instruments to mitigate non-functional currency transaction exposure on certain contracts with customers and vendors. We mitigate derivative credit risk by transacting with highly rated counterparties. We have evaluated the credit and non-performance risks associated with our derivative counterparties and believe them to be insignificant at September 30, 2010. All contracts are recorded at fair value and marked-to-market at the end of each reporting period, with unrealized gains and losses being included in accumulated other comprehensive income on the Consolidated Balance Sheets for that period. See Note J for further discussion regarding our derivative instruments.

D. Acquisition

On December 15, 2009, we acquired the business and certain assets of PowerComm Inc. and its subsidiaries, Redhill Systems, Ltd., Nextron Corporation, PCG Technical Services Inc. and Concorde Metal Manufacturing Ltd (the entire business of which is referred to herein as Powell Canada). Powell Canada is headquartered in Edmonton, Alberta, Canada and provides electrical and maintenance services in western Canada. Powell Canada is also a manufacturer of switchgear and related products, primarily serving the oil and gas industry in western Canada. This acquisition

supports our strategy to expand our geographic presence into Canada, as well as increasing our service and maintenance capabilities.

We paid \$23.4 million, plus expenses of approximately \$2.4 million, for the acquisition from our existing cash and cash equivalents and assumed \$15.1 million of existing bank debt. See the table below for assets acquired and liabilities assumed. In December 2009, approximately \$2.4 million of the \$23.4 million purchase price was placed into an escrow account related to the purchase of PowerComm's 50% interest in the operations of a joint venture in Kazakhstan. This transaction closed in April 2010 and the escrow was released.

An additional contingent payment of up to approximately \$7.6 million could have been payable after March 31, 2010, based on the earnings performance of Powell Canada and PowerComm's joint venture operations in Kazakhstan for the 12-month period ended March 31, 2010 (the Earnout). We have not recorded a liability related to the Earnout as it was not earned.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The purchase price allocated to the assets acquired and liabilities assumed is based on the estimated fair value as of the acquisition date.

Additionally, the finalization of the net asset adjustment related to the Kazakhstan transaction and the calculation of the management fee agreement related to the operating results of the Kazakhstan joint venture from December 16, 2009, through March 31, 2010, as defined in the acquisition agreement, resulted in a refund to the Company of approximately \$472,000, which was received subsequent to September 30, 2010, and was recorded as a receivable at September 30, 2010, in our consolidated balance sheet. Our interest in the net assets of the 50% ownership in the joint venture is recorded at its estimated net realizable value as the Company has made a strategic decision to exit this joint venture.

Intangible assets recorded are approximately \$9.0 million and will be amortized over an estimated weighted average life of approximately 8.4 years. Goodwill was recorded at approximately \$7.2 million and will not be amortized. Goodwill represents the excess purchase price over the estimated fair value allocated to the net assets acquired and will be deductible for income tax purposes. The amount paid in excess of the fair value of the net assets acquired was to obtain an existing service and manufacturing presence in Canada and to strengthen our strategic position in the electrical power business, utilizing the combined capabilities of Powell Canada with our existing operations. See discussion of impairment in Note E.

The purchase price allocation was as follows, based on the exchange rate as of December 15, 2009 (in thousands):

| | |
|--|-----------|
| Accounts receivable | \$ 16,643 |
| Inventories | 4,180 |
| Prepaid expenses and other current assets | 3,401 |
| Property, plant and equipment | 7,863 |
| Goodwill | 7,180 |
| Intangible assets | 9,043 |
| Accounts payable and other current liabilities | (7,649) |
| Capital lease obligations | (2,667) |
| Bank debt assumed | (15,072) |
| Total purchase price | \$ 22,922 |

Operating results of Powell Canada are included in our Electrical Power Products business segment in our Consolidated Statements of Operations from December 15, 2009.

Pro forma results for Powell Canada Acquisition (Unaudited)

The unaudited pro forma data presented below reflects the results of Powell Industries, Inc. and the acquisition of Powell Canada, assuming the acquisition was completed on October 1, 2007, (in thousands, except per share data):

Year Ended September 30,

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| | 2009 | 2008 |
|---|-------------|-------------|
| Revenues | \$ 718,156 | \$ 706,830 |
| Net income attributable to Powell Industries, Inc. | 34,077 | 21,678 |
| Earnings per share attributable to Powell Industries, Inc.: | | |
| Basic | \$ 2.98 | \$ 1.92 |
| Diluted | \$ 2.94 | \$ 1.89 |

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Pro forma results for fiscal year 2010 are not included above as the results would not be materially different from the actual results reported, as the results of Powell Canada are included in our consolidated financial statements for 91/2 months.

The unaudited pro forma information includes operating results of Powell Canada prior to the acquisition date adjusted to include the pro forma impact of the following:

- 1) Impact of interest expense as a result of increased borrowings to fund the purchase price;
- 2) Elimination of the operating results of certain businesses to be disposed of;
- 3) Impact of amortization expense related to intangible assets; and
- 4) Adjustment to record no income tax benefit from the losses of Powell Canada.

The unaudited pro forma results above do not purport to be indicative of the results that would have been obtained if the acquisitions had occurred as of the beginning of the periods presented or that may be obtained in the future.

E. Goodwill and Other Intangible Assets

Our intangible assets consist of (1) goodwill, which is not being amortized, and (2) customer relationships (15 years), trademarks (15 years), trade names (10 years), non-compete agreements (5 years), a supply agreement (15 years) and purchased technologies (6 to 7 years) which are amortized over their estimated useful lives. We test for impairment of goodwill annually, or immediately if conditions indicate that impairment could exist.

During the year ended September 30, 2010, we acquired intangible assets and recorded goodwill in connection with our acquisition of Powell Canada and our acquisition of a 50% interest in the operations of a joint venture in Kazakhstan. See Note D for additional information regarding the acquisition. During fiscal year 2010, our impairment analyses for goodwill indicated that an impairment was required. A loss on impairment of approximately \$7.5 million was recorded in fiscal year 2010 related to the Powell Canada acquisition. The Company's strategic decision to exit the 50% owned joint venture in Kazakhstan and delays in the anticipated growth in capital investments in the Oil Sands Region of western Canada, relative to our expectations, resulted in the impairment charge. No impairment was identified as a result of performing our annual impairment test for fiscal years 2009 or 2008.

Changes in our goodwill and intangible assets balances for the years ended September 30, 2010 and 2009, consisted of the following (in thousands):

| | Goodwill | Intangible Assets |
|---|-----------------|--------------------------|
| Balance at September 30, 2008 | \$ 1,084 | \$ 25,014 |
| Amortization | | (3,460) |
| Foreign currency translation adjustment | | (249) |
| Balance at September 30, 2009 | 1,084 | 21,305 |

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| | | | |
|---|----------|----|---------|
| Acquisition of Powell Canada | 7,180 | | 9,043 |
| Amortization | | | (4,477) |
| Impairment | (7,452) | | |
| Foreign currency translation adjustment | 272 | | 261 |
| Other | (81) | | |
| Balance at September 30, 2010 | \$ 1,003 | \$ | 26,132 |

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

All goodwill and intangible assets disclosed above are reported in our Electrical Power Products business segment.

Amortization of intangible assets recorded for the years ended September 30, 2010, 2009 and 2008, was approximately \$4.5 million, \$3.5 million and \$3.6 million, respectively.

Estimated amortization expense for each of the five subsequent fiscal years is expected to be (in thousands):

| Years Ending September 30, | Total |
|-----------------------------------|--------------|
| 2011 | \$ 3,444 |
| 2012 | 2,422 |
| 2013 | 2,209 |
| 2014 | 1,473 |
| 2015 | 1,375 |

F. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

| | Year Ended September 30, | | |
|---|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| <i>Numerator:</i> | | | |
| Net income attributable to Powell Industries, Inc. | \$ 25,008 | \$ 39,717 | \$ 25,847 |
| <i>Denominator:</i> | | | |
| Weighted average basic shares | 11,545 | 11,424 | 11,265 |
| Dilutive effect of stock options, restricted stock and restricted stock units | 148 | 167 | 187 |
| Weighted average diluted shares with assumed conversions | 11,693 | 11,591 | 11,452 |
| <i>Net earnings per share:</i> | | | |
| Basic | \$ 2.17 | \$ 3.48 | \$ 2.29 |
| Diluted | \$ 2.14 | \$ 3.43 | \$ 2.26 |

All options were included in the computation of diluted earnings per share for the years ended September 30, 2010, 2009 and 2008, respectively, as the options exercise prices were less than the average market price of our common stock.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****G. Detail of Selected Balance Sheet Accounts***Allowance for Doubtful Accounts*

Activity in our allowance for doubtful accounts receivable consisted of the following (in thousands):

| | September 30, | |
|--|----------------------|-------------|
| | 2010 | 2009 |
| Balance at beginning of year | \$ 1,607 | \$ 1,180 |
| Increase to bad debt expense | 422 | 959 |
| Deductions for uncollectible accounts written off, net of recoveries | (1,168) | (631) |
| Increase due to foreign currency translation | 46 | 99 |
| Balance at end of year | \$ 907 | \$ 1,607 |

Warranty Accrual

Activity in our product warranty accrual consisted of the following (in thousands):

| | September 30, | |
|--|----------------------|-------------|
| | 2010 | 2009 |
| Balance at beginning of year | \$ 7,558 | \$ 6,793 |
| Increase to warranty expense | 1,118 | 5,124 |
| Deductions for warranty charges | (2,703) | (4,008) |
| Decrease due to foreign currency translation | (44) | (351) |
| Balance at end of year | \$ 5,929 | \$ 7,558 |

Inventories

The components of inventories are summarized below (in thousands):

| | September 30, | |
|---|----------------------|-------------|
| | 2010 | 2009 |
| Raw materials, parts and subassemblies | \$ 40,325 | \$ 43,968 |
| Work-in-progress | 4,646 | 8,597 |
| Provision for excess and obsolete inventory | (6,727) | (6,313) |

| | | |
|-------------------|-----------|-----------|
| Total inventories | \$ 38,244 | \$ 46,252 |
|-------------------|-----------|-----------|

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)*****Cost and Estimated Earnings on Uncompleted Contracts***

The components of costs and estimated earnings and related amounts billed on uncompleted contracts are summarized below (in thousands):

| | September 30, | |
|---|----------------------|-------------|
| | 2010 | 2009 |
| Costs incurred on uncompleted contracts | \$ 482,149 | \$ 552,805 |
| Estimated earnings | 138,836 | 136,603 |
| | 620,985 | 689,408 |
| Less: Billings to date | 613,930 | 687,845 |
| Net underbilled position | \$ 7,055 | \$ 1,563 |
| Included in the accompanying balance sheets under the following captions: | | |
| Costs and estimated earnings in excess of billings on uncompleted contracts underbilled | \$ 38,064 | \$ 46,335 |
| Billings in excess of costs and estimated earnings on uncompleted contracts overbilled | (31,009) | (44,772) |
| Net underbilled position | \$ 7,055 | \$ 1,563 |

Property, Plant and Equipment

Property, plant and equipment are summarized below (in thousands):

| | September 30, | | Range of |
|--|----------------------|-------------|--------------------|
| | 2010 | 2009 | Asset Lives |
| Land | \$ 7,641 | \$ 7,268 | |
| Buildings and improvements | 52,627 | 51,056 | 3 - 39 Years |
| Machinery and equipment | 61,877 | 51,977 | 3 - 15 Years |
| Furniture and fixtures | 3,332 | 3,050 | 3 - 10 Years |
| Construction in process | 1,384 | 3,771 | |
| | 126,861 | 117,122 | |
| Less: Accumulated depreciation | (63,185) | (56,086) | |
| Total property, plant and equipment, net | \$ 63,676 | \$ 61,036 | |

Included in property and equipment are assets under capital lease of approximately \$4.2 million and \$246,000 at September 30, 2010 and 2009, with related accumulated depreciation of approximately \$2.2 million and \$246,000, respectively. Depreciation expense, including the depreciation of capital leases, was approximately \$9.2 million, \$7.5 million and \$8.1 million for fiscal years 2010, 2009 and 2008, respectively.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****H. Long-Term Debt**

Long-term debt consisted of the following (in thousands):

| | September 30, | |
|---|----------------------|-------------|
| | 2010 | 2009 |
| Industrial development revenue bonds | \$ 4,800 | \$ 5,200 |
| Capital lease obligations | 2,085 | |
| Deferred acquisition payable | | 4,292 |
| Subtotal long-term debt and capital lease obligations | 6,885 | 9,492 |
| Less current portion | (1,683) | (4,692) |
| Total long-term debt and capital lease obligations | \$ 5,202 | \$ 4,800 |

The annual maturities of long-term debt as of September 30, 2010, were as follows (in thousands):

| Year Ending September 30, | Long-Term Debt Maturities |
|----------------------------------|--|
| 2011 | \$ 1,683 |
| 2012 | 917 |
| 2013 | 662 |
| 2014 | 423 |
| 2015 | 400 |
| Thereafter | 2,800 |
| Total long-term debt maturities | \$ 6,885 |

US and UK Revolvers

In December 2007 and 2008, we amended our existing credit agreement (Amended Credit Agreement) with a major domestic bank and certain other financial institutions. These amendments to our credit facility were made to expand our US borrowing capacity to provide additional working capital support for the Company. The Amended Credit Agreement provides for a 1) \$58.5 million revolving credit facility (US Revolver); 2) £4.0 million (pound sterling) (approximately \$6.3 million) revolving credit facility (UK Revolver) and 3) £6.0 million (approximately \$9.5 million) single advance term loan (UK Term Loan). The UK Term Loan was repaid in September 2009 and may not be reborrowed. Expenses associated with the issuance of the original credit agreement are classified as deferred loan costs, totaled \$576,000 and are being amortized as a non-cash charge to interest expense. Obligations are

collateralized by the stock of certain of our subsidiaries.

The interest rate for amounts outstanding under the Amended Credit Agreement for the US Revolver is a floating rate based upon the higher of the Federal Funds Rate plus 0.5%, or the bank's prime rate. Once the applicable rate is determined, a margin ranging from negative 0.5% to 0.5%, as determined by our consolidated leverage ratio, is added to the applicable rate. The floating interest rate for amounts outstanding under the Amended Credit Agreement for the UK Revolver is a floating rate based upon the LIBOR plus a margin which can range from 1.25% to 2.25%, as determined by our consolidated leverage ratio as defined within the Amended Credit Agreement.

The US Revolver and the UK Revolver provide for the issuance of letters of credit which would reduce the amounts available under the respective revolvers. The amount available under the US Revolver was reduced by approximately \$15.2 million for our outstanding letters of credit at September 30, 2010. There were no letters of credit outstanding under the UK Revolver.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

There were no borrowings under the US Revolver or the UK Revolver as of September 30, 2010. Amounts available under the US Revolver and the UK Revolver were approximately \$43.3 million and \$6.3 million, respectively, at September 30, 2010. The US Revolver and the UK Revolver expire on December 31, 2012.

The Amended Credit Agreement contains certain restrictive and maintenance-type covenants, including a restriction on our ability to pay dividends. It also contains financial covenants defining various financial measures and the levels of these measures with which we must comply, as well as a material adverse change clause. A material adverse change is defined as a material change in our operations, business, properties, liabilities or condition (financial or otherwise) or a material impairment of our ability to perform our obligations under our credit agreements.

The Amended Credit Agreement's principal financial covenants include:

Minimum Tangible Net Worth The Amended Credit Agreement requires consolidated tangible net worth (stockholders' equity, less intangible assets) as of the end of each quarter to be greater than the sum of \$172,500,000, plus an amount equal to 50% of our consolidated net income for each fiscal quarter, plus an amount equal to 100% of the aggregate increase in stockholders' equity by reason of the issuance and sale of any equity interests.

Minimum Fixed Charge Coverage Ratio The Amended Credit Agreement requires that the consolidated fixed charge coverage ratio be greater than 1.25 to 1.00. The consolidated fixed charge calculation is income before interest and income taxes, increased by depreciation and amortization expense (EBITDA) and reduced by income taxes and capital expenditures for the previous 12 months, divided by the sum of payments on long-term debt, excluding the US Revolver and the UK Revolver and interest expense, during the previous 12 months.

Maximum Leverage Ratio The Amended Credit Agreement requires that the ratio be less than 2.75 to 1.00 for the quarter ended September 30, 2010, and thereafter. The maximum leverage ratio is the sum of total long-term debt and outstanding letters of credit, less industrial development revenue bonds, divided by the EBITDA for the previous 12 months.

The Amended Credit Agreement is collateralized by a pledge of 100% of the voting capital stock of each of our domestic subsidiaries and 66% of the voting capital stock of each non-domestic subsidiary, excluding Powell Canada. The Amended Credit Agreement provides for customary events of default and carries cross-default provisions with other existing debt agreements. If an event of default (as defined in the Amended Credit Agreement) occurs and is continuing, on the terms and subject to the conditions set forth in the Amended Credit Agreement, amounts outstanding under the Amended Credit Agreement may be accelerated and may become immediately due and payable. As of September 30, 2010, we were in compliance with all of the financial covenants of the Amended Credit Agreement.

Canadian Revolver

On December 15, 2009, we entered into a credit agreement with a major international bank (the Canadian Facility) to finance the \$15.1 million debt assumed in the acquisition of Powell Canada, and to provide additional working capital support for our operations in Canada. The Canadian Facility provides for a \$20 million CAD (approximately \$19.4 million) revolving credit facility (the Canadian Revolver), subject to certain limitations including a limitation on borrowings based upon certain financial ratios, as defined in the credit agreement. Expenses associated with the Canadian Facility were approximately \$0.1 million and are classified as deferred loan costs in other assets and are

being amortized as a non-cash charge to interest expense over two years.

The Canadian Revolver provides for the issuance of letters of credit which reduce the amounts which may be borrowed under the Canadian Revolver. As of September 30, 2010, there were no letters of credit outstanding under the Canadian Revolver.

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POWELL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

There were no borrowings outstanding under the Canadian Revolver, and approximately \$14.4 million was available at September 30, 2010. The amount available under the Canadian Revolver was reduced to approximately \$14.4 million based upon the available borrowing base as defined in the Canadian Facility credit agreement. The Canadian Facility expires on February 29, 2012. The interest rate for amounts outstanding under the Canadian Revolver is a floating interest rate based upon either the Canadian Prime Rate, or the lender's US Bank Rate. Once the applicable rate is determined, a margin of 0.375% to 1.125%, as determined by our consolidated leverage ratio is added to the applicable rate.

The principal financial covenants are consistent with those described in our US Revolver facility above. As discussed above, the borrowings under the Canadian Revolver are subject to a borrowing base limitation. The Canadian Facility contains a material adverse effect clause. A material adverse effect is defined as a material change in the operations of Powell or Powell Canada in relation to our financial condition, property, business operations, expected net cash flows, liabilities or capitalization.

The Canadian Facility is secured by the assets of our Canadian operations and provides for customary events of default and carries cross-default provisions with our existing debt agreements. If an event of default (as defined in the Canadian Facility credit agreement) occurs and is continuing, on the terms and subject to the conditions set forth in the Canadian Facility credit agreement, amounts outstanding under the Canadian Facility may be accelerated and may become immediately due and payable. As of September 30, 2010, we were in compliance with all of the financial covenants of the Canadian Facility credit agreement.

Canadian Term Loan

The Canadian Facility also provided for a single advance term loan of \$2.5 million CAD (approximately \$2.3 million) (the Canadian Term Loan). The Canadian Term Loan provided a single advance of \$2.4 million for financing the acquisition of Powell Canada. The Canadian Term Loan was repaid in September 2010 and may not be reborrowed.

Industrial Development Revenue Bonds

We borrowed \$8.0 million in October 2001 through a loan agreement funded with proceeds from tax-exempt industrial development revenue bonds (Bonds). These Bonds were issued by the Illinois Development Finance Authority and were used for the completion of our Northlake, Illinois, facility. Pursuant to the Bond issuance, a reimbursement agreement between us and a major domestic bank required an issuance by the bank of an irrevocable direct-pay letter of credit (Bond LC) to the Bonds' trustee to guarantee payment of the Bonds' principal and interest when due. The Bond LC is subject to both early termination and extension provisions customary to such agreements, as well as various covenants, for which we are in compliance at September 30, 2010. While the Bonds mature in 2021, the reimbursement agreement requires annual redemptions of \$400,000 that commenced on October 25, 2002. A sinking fund is used for the redemption of the Bonds. At September 30, 2010, the balance in the restricted sinking fund was approximately \$434,000 and was recorded in cash and cash equivalents. The Bonds bear interest at a floating rate determined weekly by the Bonds' remarketing agent, which was the underwriter for the Bonds and is an affiliate of the bank. This interest rate was 0.55% per year on September 30, 2010.

Deferred Acquisition Payable

In connection with the acquisition of the Power/Vac[®] product line, \$8.5 million of the total purchase price of \$32.0 million was paid to General Electric Company at closing on August 7, 2006. The remaining balance of the purchase price of \$23.5 million was payable in four installments every 10 months over the 40 months following the acquisition date, with the final installment being paid in December 2009. At September 30, 2010, there was no balance remaining related to the deferred acquisition payable.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****I. Income Taxes**

The components of the income tax provision were as follows (in thousands):

| | Year Ended September 30, | | |
|----------------------------|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| Current: | | | |
| Federal | \$ 18,126 | \$ 18,028 | \$ 10,487 |
| State | 1,750 | 2,910 | 1,628 |
| Foreign | 1,071 | 1,146 | 1,601 |
| Deferred | (1,053) | (1,350) | 356 |
| Total income tax provision | \$ 19,894 | \$ 20,734 | \$ 14,072 |

Income before interest, income taxes and minority interest was as follows (in thousands):

| | Year Ended September 30, | | |
|---|---------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| U.S. | \$ 53,467 | \$ 56,115 | \$ 35,089 |
| Other than U.S. | (8,406) | 4,544 | 4,779 |
| Income from continuing operations before provision for income taxes | \$ 45,061 | \$ 60,659 | \$ 39,868 |

A reconciliation of the statutory U.S. income tax rate and the effective income tax rate, as computed on earnings before income tax provision in each of the three years presented in the Consolidated Statements of Operations, was as follows:

| | Year Ended September 30, | | |
|--|-------------------------------------|-------------|-------------|
| | 2010 | 2009 | 2008 |
| Statutory rate | 35% | 35% | 35% |
| State income taxes, net of federal benefit | 3 | 3 | 3 |
| International withholding tax | | (1) | |
| Other permanent tax items | | | (1) |
| Foreign rate differential | 1 | (1) | (1) |
| Domestic production activities deduction | (2) | (2) | (1) |
| Foreign valuation allowance and other | 7 | | |

| | | | |
|----------------|-----|-----|-----|
| Effective rate | 44% | 34% | 35% |
|----------------|-----|-----|-----|

Our provision for income taxes reflects an effective tax rate on earnings before income taxes of 44% in fiscal year 2010 compared to 34% and 35% in fiscal years 2009 and 2008, respectively. The increase in the effective tax rate resulted from a valuation allowance against deferred tax assets in Canada.

We have not recorded deferred income taxes on approximately \$20.0 million of undistributed earnings of our foreign subsidiaries because of management's intent to indefinitely reinvest such earnings. Upon distribution of these earnings in the form of dividends or otherwise, we may be subject to U.S. income taxes and foreign withholding taxes. It is not practical, however, to estimate the amount of taxes that may be payable on the eventual remittance of these earnings.

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We are subject to income tax in the United States, multiple state jurisdictions and a few international jurisdictions, primarily the United Kingdom and in Canada as of December 15, 2009. For United States Federal income tax purposes, all years prior to 2007 are closed. The Internal Revenue Service (IRS) recently completed an examination of the returns for the 2005 and 2006 tax years. No material adjustments were identified during the examination. We do not consider any state in which we do business to be a major tax jurisdiction. We remain open to examination in the United Kingdom for tax years 2008 to the present.

The net deferred income tax asset (liability) was comprised of the following (in thousands):

| | September 30, | |
|--|----------------------|-------------|
| | 2010 | 2009 |
| Current deferred income taxes: | | |
| Gross assets | \$ 8,057 | \$ 9,457 |
| Gross liabilities | (4,970) | (6,154) |
| Net current deferred income tax asset | 3,087 | 3,303 |
| Noncurrent deferred income taxes: | | |
| Gross assets | 7,721 | 3,894 |
| Gross liabilities | (5,634) | (2,703) |
| Net noncurrent deferred income tax asset | 2,087 | 1,191 |
| Net deferred income tax asset | \$ 5,174 | \$ 4,494 |

At September 30, 2010 and 2009, the noncurrent deferred income tax asset was included in other assets on the Consolidated Balance Sheets.

The tax effect of temporary differences between GAAP accounting and federal income tax accounting creating deferred income tax assets and liabilities were as follows (in thousands):

| | September 30, | |
|---------------------------------------|----------------------|-------------|
| | 2010 | 2009 |
| Allowance for doubtful accounts | \$ 110 | \$ 40 |
| Workers compensation | 200 | 388 |
| Stock-based compensation | 390 | 458 |
| Reserve for accrued employee benefits | 1,638 | 2,431 |
| Warranty accrual | 1,672 | 2,900 |
| Uncompleted long-term contracts | (4,164) | (6,155) |
| Depreciation and amortization | 1,291 | (627) |

| | | |
|--|----------|----------|
| Deferred compensation | 999 | 1,062 |
| Postretirement benefits liability | 350 | 396 |
| Accrued legal | 88 | 93 |
| Uniform capitalization and inventory | 3,813 | 3,495 |
| Software development costs | (461) | (488) |
| Goodwill impairment | 2,122 | |
| Net operating loss | 903 | |
| Valuation allowance on foreign deferred tax assets | (3,729) | |
| Other | (48) | 501 |
| Net deferred income tax asset | \$ 5,174 | \$ 4,494 |

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

At September 30, 2010, we had approximately \$2.7 million of foreign net operating loss carryforward, which is subject to a 20-year carryforward. During the fourth quarter of the fiscal year ended September 30, 2010, we recorded a valuation allowance of \$3.7 million against our Canadian deferred tax assets, which we expect cannot be realized through future reversals of existing taxable temporary differences and our estimate of future taxable income. We believe that our deferred tax assets in other tax jurisdictions are more likely than not realizable through future reversals of existing taxable temporary differences and our estimate of future taxable income.

In the first quarter of fiscal year 2008, we adopted accounting guidance on the accounting for uncertainty in income taxes. Upon adoption of the guidance, we recorded a \$0.3 million increase in our tax reserves, an offsetting decrease of \$0.2 million to retained earnings for uncertain tax positions and an increase in deferred income tax assets of \$0.1 million. As of the adoption date, we had total tax reserves of approximately \$1.2 million. This reserve includes an estimate of potential interest and penalties on estimated liabilities for uncertain tax positions, which were recorded as components of income tax expense, in the amount of \$135,000 as of September 30, 2010. A reconciliation of the beginning and ending amount of the unrecognized tax benefits follows (in thousands):

| | |
|--|--------|
| Balance as of September 30, 2009 | \$ 588 |
| Increases related to tax positions taken during a prior period | 331 |
| Decreases related to expectations of statute of limitations | (78) |
| Balance as of September 30, 2010 | \$ 841 |

Our continuing policy is to recognize interest and penalties related to income tax matters as tax expense. The amount of interest and penalty expense recorded for the year ended September 30, 2010, was not material.

There was no material change in the net amount of unrecognized tax benefits in the year ended September 30, 2010. Management believes that it is reasonably possible that within the next 12 months, the total unrecognized tax benefits will decrease by approximately 1% due to the expiration of certain statutes of limitations in various state and local jurisdictions.

Management believes that an adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in our tax audits are resolved in a manner not consistent with management's expectations, we could be required to adjust our provision for income tax in the period such resolution occurs. Although timing of the resolution and/or closure of audits is highly uncertain, we do not believe it is reasonably possible that our unrecognized tax benefits would materially change in the next 12 months.

J. Derivative Instruments and Hedging Strategies

We operate in various countries and have operations in the United Kingdom and Canada. These international operations expose us to market risk associated with foreign currency exchange rate fluctuations. We have entered into certain forward contracts to hedge the risk of certain foreign currency rate fluctuations. To the extent we choose to manage volatility associated with the net exposures, we enter into various financial transactions which we account for using the applicable accounting guidance for derivative instruments and hedging activities. Our objective is to hedge

the variability in forecasted cash flow due to the foreign currency risk associated with certain long-term sales. As of September 30, 2010, we held only derivatives that were designated as cash flow hedges related to the U.S. Dollar/British Pound Sterling exchange rate.

In order for a derivative to qualify for hedge accounting, the derivative must be formally designated as a hedge by documenting the relationship between the derivative and the hedged item. The documentation includes a description of the hedging instrument, the hedge item, the risk being hedged, our risk management objective and strategy for undertaking the hedge, the method for assessing the effectiveness of the hedge and the method for measuring hedge ineffectiveness. Additionally, the hedge relationship must be expected to be highly effective at offsetting changes in either the fair value or cash flows of the hedged item at both inception of the hedge and on an

Table of Contents**POWELL INDUSTRIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

ongoing basis. We assess the ongoing effectiveness of our hedges in accordance with the Cumulative Dollar-Offset Approach, and measure and record hedge ineffectiveness at the end of each fiscal quarter, as necessary.

All derivatives are recognized on the Consolidated Balance Sheets at their fair value and classified based on the instrument's maturity date. The total notional amount of outstanding derivatives as of September 30, 2010, was approximately \$1.5 million.

The following table presents the fair value of derivative instruments included with the Consolidated Balance Sheets as of September 30, 2010:

| | Asset Derivatives | | Liability Derivatives | |
|--|---|-----------------------|-------------------------------|-------------------|
| | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| | | (In thousands) | | |
| Derivatives designated as hedging instruments: | | | | |
| Foreign exchange forwards | Prepaid expenses and other current assets | \$ | Other accrued expenses | \$ 47 |
| Total derivatives | | \$ | | \$ 47 |

The following table presents the fair value of derivative instruments included with the Consolidated Balance Sheets as of September 30, 2009:

| | Asset Derivatives | | Liability Derivatives | |
|--|---|-----------------------|-------------------------------|-------------------|
| | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| | | (In thousands) | | |
| Derivatives designated as hedging instruments: | | | | |
| Foreign exchange forwards | Prepaid expenses and other current assets | \$ | Other accrued expenses | \$ 752 |
| Foreign exchange forwards | Deferred income taxes | 164 | Other liabilities | |
| Total derivatives | | \$ 164 | | \$ 752 |

The following table presents the amounts affecting the Consolidated Statements of Operations for the year ended September 30, 2010:

| | Amount of Gain (Loss) Recognized in Other Comprehensive Income on Derivatives(1) Year Ended September 30, 2010 | Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income | Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income(1) Year Ended <i>A protracted economic slowdown and rising unemployment could harm our business.</i> |
|-------------------------------|---|---|--|
| Derivatives Designated | | | |

We believe that many students pursue post-secondary education to be more competitive in the job market. However, a protracted economic slowdown could increase unemployment and diminish job prospects generally. Diminished job prospects and heightened financial worries could affect the willingness of students to incur loans to pay for post-secondary education and to pursue post-secondary education in general. As a result, our enrollments could suffer.

We may incur costs in complying with the Americans with Disabilities Act and with similar laws.

The Americans with Disabilities Act of 1990, or ADA, requires all public accommodations to meet federal requirements for access and use by disabled individuals. Other federal, state, and local laws and regulations also

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may impose similar or additional accessibility requirements. For example, the Fair Housing Amendments Act of 1988, or FHAA, requires apartment properties first occupied after March 13, 1991, to be accessible to handicapped persons. Typically, our real estate leases require us to pay any costs necessary to comply with all laws, including these accessibility laws, for our premises, which may include parking areas, restaurants at our culinary schools, dormitory facilities and similar facilities in addition to classroom and office space. In opening new schools or locations and acquiring existing schools, we often must build out the premises to satisfy our classroom needs and must incur the costs associated with accessibility compliance in those construction activities. If any of our premises are not compliant with the ADA or FHAA, we could face fines, litigation by private litigants, and orders to correct any non-complying features.

Risk Related to Our Common Stock

The trading price of our common stock may fluctuate substantially in the future.

The trading price of our common stock may fluctuate substantially as a result of a number of factors, some of which are not in our control. These factors include:

changes in the student lending and credit markets;

our ability to meet or exceed expectations of analysts or investors;

quarterly variations in our operating results;

changes in the legal or regulatory environment in which we operate;

general conditions in the post-secondary education field, including changes in the ED, state laws and regulations and accreditation standards, or availability of student financing;

the initiation, pendency or outcome of litigation, regulatory reviews and investigations, and any related adverse publicity;

changes in our earnings estimates by analysts;

future impairment of goodwill or other intangible assets;

price and volume fluctuations in the overall stock market, which have particularly affected the market prices of many companies that provide post-secondary education in recent periods;

the loss of key personnel; and

general economic conditions.

These factors may adversely affect the trading price of our common stock, regardless of our actual operating performance, and could prevent an investor from selling shares of our common stock at or above the price at which the investor acquired the shares. In addition, the stock markets, from time to time, experience extreme price and volume fluctuations that may be unrelated or disproportionate to the operating performance of

companies. These broad fluctuations may adversely affect the market price of our common stock, regardless of our operating performance.

Table of Contents**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table sets forth information regarding purchases made by us of shares of our common stock on a monthly basis during the six months, June 30, 2009:

Issuer Purchases of Equity Securities

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1) | Maximum Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1) |
|--------------------------------------|----------------------------------|------------------------------|--|--|
| January 1, 2009 – January 31, 2009 | | \$ | | \$ 195,466,742 |
| February 1, 2009 – February 28, 2009 | 506,400 | 24.74 | 506,400 | 182,940,464 |
| March 1, 2009 – March 31, 2009 | 1,245,832 | 22.05 | 1,245,832 | 155,469,103 |
| April 1, 2009 – April 30, 2009 | | | | 155,469,103 |
| May 1, 2009 – May 31, 2009 | 3,588,147 | 20.65 | 3,588,147 | 81,378,795 |
| June 1, 2009 – June 30, 2009 | 1,245,795 | 20.80 | 1,245,795 | 55,469,344 |
| Total | 6,586,174 | | 6,586,174 | |

- (1) As of June 30, 2009, our Board of Directors had authorized us to use up to approximately \$800.2 million for the repurchase of shares of our outstanding common stock. Pursuant to this stock repurchase program, we may repurchase shares of our outstanding common stock on the open market or in private transactions from time to time, depending on factors including market conditions and corporate and regulatory requirements. The stock repurchase program does not have an expiration date and may be suspended or discontinued at any time. On August 4, 2009, our Board of Directors authorized the use of an additional \$200.0 million to repurchase outstanding shares of our common stock. This is in addition to the \$55.5 million available under the program as of June 30, 2009.

Item 6. Exhibits*(a)* Exhibits

- 31.1 Certification of CEO pursuant to Section 302 of Sarbanes-Oxley Act of 2002
31.2 Certification of CFO pursuant to Section 302 of Sarbanes-Oxley Act of 2002
32.1 Certification of CEO pursuant to Section 906 of Sarbanes-Oxley Act of 2002
32.2 Certification of CFO pursuant to Section 906 of Sarbanes-Oxley Act of 2002

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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.

CAREER EDUCATION CORPORATION

Date: August 5, 2009

By: /s/ GARY E. McCULLOUGH
Gary E. McCullough
President and Chief Executive Officer
(Principal Executive Officer)

Date: August 5, 2009

By: /s/ MICHAEL J. GRAHAM
Michael J. Graham
Executive Vice President and

Chief Financial Officer
(Principal Financial Officer)