FRANKLIN ELECTRIC CO INC
Form 10-Q
May 08, 2018

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

FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number 0-362

FRANKLIN ELECTRIC CO., INC.
(Exact name of registrant as specified in its charter)

Indiana	35-0827455
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

9255 Coverdale Road	
Fort Wayne, Indiana	46809
(Address of principal executive offices)	(Zip Code)

(260) 824-2900
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x NO o

Indicate by check mark whether the registrant 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 (Section 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 x NO o

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer x Accelerated Filer o Non-Accelerated Filer o Smaller Reporting Company o
Emerging Growth Company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

YES o NO x

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

Class of Common Stock	Outstanding at April 30, 2018
$.10 par value	46,517,589 shares

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PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except per share amounts)	First Quarter Ended March 31, 2018	March 31, 2017
Net sales	$295,630	$220,252
Cost of sales	196,648	144,436
Gross profit	98,982	75,816
Selling, general, and administrative expenses	76,275	56,996
Restructuring expense	7	315
Operating income	22,700	18,505
Interest expense	(2,428)	(3,514)
Other income/(expense), net	(204)	672
Foreign exchange income/(expense)	(551)	475
Income before income taxes	19,517	16,138
Income tax (benefit)/expense	(1,698)	204
Net income	$21,215	$15,934
Less: Net income attributable to noncontrolling interests	(41)	(204)
Net income attributable to Franklin Electric Co., Inc.	$21,174	$15,730
Income per share:		
Basic	$0.45	$0.33
Diluted	$0.45	$0.33
Dividends per common share	$0.1075	$0.1000

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(In thousands)	First Quarter Ended March 31, 2018	March 31, 2017
Net income	$21,215	$15,934
Other comprehensive income, before tax:		
Foreign currency translation adjustments	6,995	8,403
Employee benefit plan activity	778	743
Other comprehensive income	7,773	9,146
Income tax expense related to items of other comprehensive income	(177)	(252)
Other comprehensive income, net of tax	7,596	8,894
Comprehensive income	28,811	24,828
Less: Comprehensive income attributable to noncontrolling interests	93	211
Comprehensive income attributable to Franklin Electric Co., Inc.	$28,718	$24,617

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands)	March 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$67,370	$67,233
Receivables, less allowances of $5,052 and $4,430, respectively	192,771	171,007
Inventories:		
Raw material	121,743	109,590
Work-in-process	18,695	16,742
Finished goods	202,878	185,993
Total inventories	343,316	312,325
Other current assets	38,394	38,566
Total current assets	641,851	589,131
Property, plant, and equipment, at cost:		
Land and buildings	144,854	142,088
Machinery and equipment	272,405	268,373
Furniture and fixtures	49,290	52,916
Other	26,509	22,810
Property, plant, and equipment, gross	493,058	486,187
Less: Allowance for depreciation	(275,690)	(270,493)
Property, plant, and equipment, net	217,368	215,694
Deferred income taxes	9,212	8,929
Intangible assets, net	129,918	131,471
Goodwill	239,000	236,810
Other assets	3,315	3,318
Total assets	$1,240,664	$1,185,353

	March 31, 2018	December 31, 2017
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$84,829	$79,348
Accrued expenses and other current liabilities	48,196	63,887
Income taxes	2,747	2,213
Current maturities of long-term debt and short-term borrowings	152,945	100,453
Total current liabilities	288,717	245,901
Long-term debt	125,076	125,596
Income taxes payable non-current	17,391	17,391
Deferred income taxes	26,021	30,913
Employee benefit plans	41,058	42,178
Other long-term liabilities	18,485	19,251
Commitments and contingencies (see Note 15)	—	—
Redeemable noncontrolling interest	1,360	1,502
Shareholders' equity:		
Common stock (65,000 shares authorized, $.10 par value) outstanding (46,522 and 46,630, respectively)	4,652	4,663
Additional capital	244,095	240,136
Retained earnings	613,113	604,905
Accumulated other comprehensive loss	(141,503)	(149,047)
Total shareholders' equity	720,357	700,657
Noncontrolling interest	2,199	1,964
Total equity	722,556	702,621
Total liabilities and equity	$1,240,664	$1,185,353

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	Three Months Ended March 31, 2018	March 31, 2017
Cash flows from operating activities:		
Net income	$21,215	$15,934
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	9,896	8,924
Share-based compensation	3,326	2,941
Deferred income taxes	(5,417)	(1,483)
(Gain)/loss on disposals of plant and equipment	(396)	79
Foreign exchange (income)/expense	551	(475)
Changes in assets and liabilities, net of acquisitions		
Receivables	(17,242)	(6,560)
Inventory	(23,932)	(29,661)
Accounts payable and accrued expenses	(15,378)	(10,539)
Income taxes	(2,463)	(2,002)
Employee benefit plans	(786)	(1,230)
Other, net	3,442	(499)
Net cash flows from operating activities	(27,184)	(24,571)
Cash flows from investing activities:		
Additions to property, plant, and equipment	(5,921)	(4,908)
Proceeds from sale of property, plant, and equipment	208	34
Cash paid for acquisitions, net of cash acquired	(8,428)	—
Other, net	—	(7)
Net cash flows from investing activities	(14,141)	(4,881)
Cash flows from financing activities:		
Proceeds from issuance of debt	59,561	20,383
Repayment of debt	(7,554)	(20,843)
Proceeds from issuance of common stock	642	481
Purchases of common stock	(7,949)	(665)
Dividends paid	(5,037)	(4,668)
Net cash flows from financing activities	39,663	(5,312)
Effect of exchange rate changes on cash	1,799	1,084
Net change in cash and equivalents	137	(33,680)
Cash and equivalents at beginning of period	67,233	104,331
Cash and equivalents at end of period	$67,370	$70,651

(In thousands)	Three Months Ended March 31, 2018	March 31, 2017
Cash paid for income taxes, net of refunds	$6,029	$4,165
Cash paid for interest	$2,502	$2,312
Non-cash items:		
Additions to property, plant, and equipment, not yet paid	$—	$530
Payable to seller of Bombas Leao	$—	$24
Payable to seller of Valley Farms Supply, Inc.	$450	$—

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN ELECTRIC CO., INC. AND CONSOLIDATED SUBSIDIARIES
INDEX TO NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
The accompanying condensed consolidated balance sheet as of December 31, 2017, which has been derived from audited financial statements, and the unaudited interim condensed consolidated financial statements as of March 31, 2018, and for the first quarters ended March 31, 2018 and March 31, 2017 have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to those rules and regulations. In the opinion of management, all accounting entries and adjustments (including normal, recurring adjustments) considered necessary for a fair presentation of the financial position and the results of operations for the interim period have been made. Operating results for the first quarter ended March 31, 2018 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2018. For further information, including a description of the critical accounting policies of Franklin Electric Co., Inc. (the "Company"), refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

2. ACCOUNTING PRONOUNCEMENTS
Adoption of New Accounting Standards
In March 2017, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2017-07, Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. This ASU requires entities to present only the service cost component of net periodic benefit cost as an operating expense (consistent with the presentation of other employee compensation costs). The other components of net periodic benefit cost are to be presented as a non-operating expense. The Company adopted ASU 2017-07 during the first quarter ended March 31, 2018. The prior year non-service cost component of net periodic benefit costs as of March 31, 2017 was less than $0.1 million and is not considered significant. The Company has included current year non-service costs as non-operating expense. The adoption of this pronouncement did not have a material impact to the Company’s condensed consolidated financial position, results of operations, or cash flows.
In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606) as modified by subsequently issued ASUs 2015-14, 2016-08, 2016-10, 2016-12 and 2016-20 (collectively ASU 2014-09). Topic 606 supersedes the revenue recognition requirements in Accounting Standards Codification (“ASC”) Topic 605, Revenue Recognition (“Topic 605”), and requires the recognition of revenue when promised goods or services are transferred to customers in an amount that reflects the considerations to which the entity expects to be entitled to in exchange for those goods or services. The Company made the accounting policy election allowed by ASC 606-10-32-2A to continue to present sales tax on a net basis, consistent with current guidance in ASC 605-45-15-2(e). The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method). The Company adopted ASU 2014-09 during the first quarter ended March 31, 2018 utilizing the modified retrospective approach. The adoption of this ASU did not have a material impact to the Company’s condensed consolidated financial position, results of operations, or cash flow; however, the adoption of this ASU requires the Company to disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The Company completed its assessment of the additional disclosure requirements with the following results:
Disaggregation of Revenue
The adoption of this ASU requires the company to disaggregate revenue into categories to depict how the nature, timing, and uncertainty of revenue and cash flows are affected by economic factors. As evidenced in Footnote 14 Segment and Geographic Information, the Company’s business consists of the Water, Fueling, Distribution, and Other segments. The Other segment includes unallocated corporate expenses and intersegment eliminations. A reconciliation

of disaggregated revenue to segment revenue as well as Water Segment revenue by geographical regions is provided in Footnote 14, consistent with how the Company evaluates financial performance.
Performance Obligations
A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in ASC Topic 606. The Company typically sells its products to customers by purchase order, and does not have any additional performance obligations included in contracts to customers other than the shipment of products. The Company records net sales revenues after discounts at the time of sale based on specific discount programs in effect, related historical data, and experience. The Company typically ships products FOB shipping at

which point control of the products passes to the customers. Any shipping and handling fees prior to shipment are considered activities required to fulfill the Company’s promise to transfer goods, and do not qualify as a separate performance obligation. Shipping and handling costs are recorded as a component of cost of sales. Additionally, the Company offers assurance-type warranties (vs. service warranties) which do not qualify as a separate performance obligation. Therefore, the Company allocates the transaction price based on a single performance obligation. The Company offers normal and customary trade terms to its customers, no significant part of which is of an extended nature. The Company considers the performance obligation satisfied and recognizes revenue at a point in time, the time of shipment. The Company does not generally allow for refunds or returns to customers and does not have outstanding performance obligations for contracts with original durations of greater than one year at the end of the reporting period.

Contract Costs

The Company does not have outstanding contracts with an original term greater than one year; therefore, the Company expenses costs to obtain a contract as incurred.

Accounting Standards Issued But Not Yet Adopted

In February 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. This ASU was issued following the enactment of the U.S. Tax Cuts and Jobs Act of 2017 and permits entities to elect a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Act. The ASU is effective for interim and annual periods beginning after December 15, 2018, with early adoption permitted, and may be applied either at the beginning of the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Act is recognized. The Company is currently assessing the impact of the ASU on the Company’s consolidated financial position, results of operations, and cash flows.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. ASU 2017-04 removes step two from the goodwill impairment test and instead requires an entity to recognize a goodwill impairment charge for the amount by which the goodwill carrying amount exceeds the reporting unit's fair value. The ASU is effective on a prospective basis for interim and annual periods beginning after December 15, 2019 with early adoption permitted. The Company is still determining the date of adoption for this ASU but does not anticipate the adoption to have a material impact on the Company's consolidated financial position, results of operations, or cash flows.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which supersedes existing guidance on accounting for leases found in Accounting Standards Codification (“ASC”) Topic 840. This ASU requires lessees to present right-of-use assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. The guidance is to be applied using a modified retrospective approach at the beginning of the earliest comparative period in the financial statements and is effective for interim and annual periods beginning after December 15, 2018 with early adoption permitted. The Company has begun the evaluation process for the adoption of the ASU, and anticipates that the majority of the Company’s outstanding operating leases would be recognized as right-of-use assets and lease liabilities upon adoption, resulting in a significant impact to the Company’s consolidated balance sheets. The Company is implementing a lease accounting software package for lease administration and compliance reporting and is in the process of entering its lease data into this package. The impact of this ASU is non-cash in nature and will not affect the Company’s cash position. The impact to the Company’s results of operations is still being evaluated.

3. ACQUISITIONS

During the first quarter ended March 31, 2018, the Company acquired 100 percent of the ownership interests of Lansing, Michigan-based Valley Farms Supply, Inc. ("Valley Farms"), for a purchase price of approximately $9.2 million. Valley Farms is a professional groundwater distributor operating three locations in the State of Michigan and one in the State of Indiana. Valley Farms was acquired to serve customers in this region of the United States as part of the Company’s Distribution Segment, which is a collection of leading groundwater distributors. The Company has not presented separate results of operations since closing or combined pro forma financial information of the Company and the acquired interest since the beginning of 2018, as results of operations for this acquisition is immaterial. During the second quarter of 2017, the Company redeemed 10 percent of the noncontrolling interest of Impo, a Turkish subsidiary, increasing the Company's ownership to 100 percent for approximately TRY 17.0 million, \$5.0 million at the then current exchange rate. The 10 percent redemption value was calculated using a specified formula and resulted in a reduction to the carrying value of TRY 0.6 million (\$0.2 million). Due to the immaterial nature of the redemption, the Company has not included full year proforma statements of income for the periods presented.

During the second quarter of 2017, the Company acquired controlling interests in three distributors (2M Company, Inc. (“2M”), Drillers Service, Inc. (“DSI”), and Western Hydro, LLC (“Western Hydro”), collectively referred to below as the “Headwater acquisitions”) in the U.S. professional groundwater market for a combined purchase price of approximately $57.4 million, subject to certain terms and conditions. The Company had previously prepaid a $3.0 million portion of the purchase price at the time of original investment. The Company funded the Headwater acquisitions with cash on hand and short-term borrowings from the Company’s Revolver (see Note 10 - Debt). The Headwater acquisitions provide the Company with a professional groundwater distribution channel throughout the United States.

The Company previously held equity interests in these entities, each of which was less than 50 percent, and accounted for by the equity method of accounting. The Company’s total interest in each of the entities is now 100 percent and the entities are included in the Company’s consolidated results effective from the date of acquisition. The original equity interests in the acquired entities were remeasured to their fair values as of the acquisition date (which aggregated was $20.6 million) based on the income approach, which utilized management estimates and consultation with an independent third-party valuation firm. Inputs included an analysis of the enterprise value based on financial projections and ownership percentages.

The preliminary identifiable intangible assets recognized due to the Headwater acquisitions were $5.7 million and consist of customer relationships, which will be amortized utilizing the straight-line method over 15 years. The fair value of the identifiable intangible assets has been estimated using an income approach, a valuation method that values an intangible asset by discounting the future incremental earnings that may be achieved by the subject intangible asset.

The preliminary goodwill of $33.9 million resulting from the Headwater acquisitions consists primarily of the benefits of forward channel integration opportunities and broadened product offerings. All of the goodwill was recorded as part of the Distribution segment, and only a portion ($7.8 million) is expected to be deductible for tax purposes.

The preliminary purchase price assigned to the major identifiable assets and liabilities for the Headwater acquisitions on an aggregated basis is as follows:

(In millions)	
Cash	$2.7
Receivables	29.9
Inventory	56.0
Other current assets	5.1
Total current assets	93.7
Property, plant, and equipment	9.8
Intangible assets	5.7
Goodwill	33.9
Other assets	0.2
Total assets	143.3
Accounts payable	(19.6)
Accrued liabilities and other current liabilities	(11.4)
Current maturities of long-term debt	(31.6)
Total current liabilities	(62.6)
Long-term debt	(2.0)
Other long-term liabilities	(0.7)
Total liabilities	(65.3)
Total	78.0
Less: Fair value of original equity interest	(20.6)
Total purchase price	$57.4

The fair values of the assets acquired and liabilities assumed related to the Headwater acquisitions are provisional amounts as of March 31, 2018, pending final valuations and purchase accounting adjustments. The Company utilized management estimates and consultation with an independent third-party valuation firm to assist in the valuation process.

The following unaudited proforma financial information for the first quarters ended March 31, 2018 and March 31, 2017 gives effect to the Headwater acquisitions by the Company as if the acquisitions had occurred as of January 1, 2017. These unaudited proforma condensed consolidated financial statements are prepared for informational purposes only and are not necessarily indicative of actual results or financial position that would have been achieved had the acquisitions been consummated on the dates indicated and are not necessarily indicative of future operating results or financial position of the consolidated companies. The unaudited proforma condensed consolidated financial statements do not give effect to any cost savings or incremental costs that may result from the integration of the Headwater acquisitions with the Company.

FRANKLIN ELECTRIC CO., INC.
PROFORMA CONDENSED CONSOLIDATED
STATEMENTS OF INCOME

(in millions, except per share amounts)	First Quarter Ended March 31, 2018	March 31, 2017
Revenue:		
As reported	$295.6	$220.3
Proforma	295.6	270.3
Net income:		
As reported	$21.2	$15.7
Proforma	21.2	16.6
Basic earnings per share:		
As reported	$0.45	$0.33
Proforma	0.45	0.35
Diluted earnings per share:		
As reported	$0.45	$0.33
Proforma	0.45	0.35

The Headwater entities contributed a total of $56.2 million of revenue and $0.9 million of net loss to the Company's condensed consolidated statements of income for the first quarter ended March 31, 2018.

Transaction costs were expensed as incurred under the guidance of FASB Accounting Standards Codification Topic 805, Business Combinations. There were $0.1 million and $0.2 million of transaction costs included in the "Selling, general, and administrative expenses" line of the Company's condensed consolidated statements of income for the first quarters ended March 31, 2018 and March 31, 2017, respectively.

4. FAIR VALUE MEASUREMENTS

FASB ASC Topic 820, Fair Value Measurements and Disclosures, provides guidance for defining, measuring, and disclosing fair value within an established framework and hierarchy. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The standard established a fair value hierarchy which requires an entity to maximize the use of observable inputs and to minimize the use of unobservable inputs when measuring fair value. The three levels of inputs that may be used to measure fair value within the hierarchy are as follows:

Level 1 – Quoted prices for identical assets and liabilities in active markets;

Level 2 – 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, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and

Level 3 – Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

As of March 31, 2018 and December 31, 2017, the assets measured at fair value on a recurring basis were as set forth in the table below:

(In millions)	March 31, 2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	$ 3.5	$ 3.5	$ —	$ —

	December 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	$ 3.0	$ 3.0	$ —	$ —

The Company's Level 1 assets consist of cash equivalents which are generally comprised of foreign bank guaranteed certificates of deposit.

The Company has no assets measured on a recurring basis classified as Level 2 or Level 3.

Total debt, including current maturities, have carrying amounts of $278.0 million and $226.0 million and estimated fair values of $280 million and $230 million as of March 31, 2018 and December 31, 2017, respectively. In the absence of quoted prices in active markets, considerable judgment is required in developing estimates of fair value. Estimates are not necessarily indicative of the amounts the Company could realize in a current market transaction. In determining the fair value of its debt, the Company uses estimates based on rates currently available to the Company for debt with similar terms and remaining maturities. Accordingly, the fair value of debt is classified as Level 2 within the valuation hierarchy.

5. FINANCIAL INSTRUMENTS

The Company’s deferred compensation stock program is subject to variable plan accounting and, accordingly, is adjusted for changes in the Company’s stock price at the end of each reporting period. The Company has entered into share swap transaction agreements ("the swap") to mitigate the Company’s exposure to the fluctuations in the Company's stock price. The swap has not been designated as a hedge for accounting purposes and is cancellable with 30 days' written notice by either party. As of March 31, 2018, the swap had a notional value based on 215,000 shares. For the first quarters ended March 31, 2018 and March 31, 2017, the swap resulted in a loss of $1.1 million and a gain of $0.8 million, respectively. Gains and losses resulting from the the swap were primarily offset by gains and losses on the fair value of the deferred compensation stock liability. All gains or losses and expenses related to the swap are recorded in the Company's condensed consolidated statements of income within the “Selling, general, and administrative expenses” line.

6. OTHER ASSETS

Through the second quarter of 2017, the Company held equity interests in the acquired companies identified in Note 3 - Acquisitions for various strategic purposes. The investments were accounted for under the equity method and were included in “Other assets” on the Company’s condensed consolidated balance sheets. The carrying amount of the investments were adjusted for the Company's proportionate share of earnings, losses, and dividends. The investments were not considered material to the Company’s financial position, either individually or in the aggregate. During the second quarter of 2017, the remaining interests of these equity method investments were purchased (see Note 3 - Acquisitions), bringing total ownership of these entities to 100 percent. As of March 31, 2018, there were no equity method investments recorded on the Company's condensed consolidated balance sheets. Prior to the purchase of the remaining interests, the Company’s proportionate share of earnings from its equity interests, were included in the "Other income, net" line of the Company's condensed consolidated statements of income. This amount was immaterial for the first quarter ended March 31, 2017.

7. GOODWILL AND OTHER INTANGIBLE ASSETS
The carrying amounts of the Company’s intangible assets are as follows:

(In millions)	March 31, 2018		December 31, 2017	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangibles:				
Patents	$7.6	$ (6.8)	$7.5	$ (6.7)
Technology	7.5	(6.0)	7.5	(5.8)
Customer relationships	139.4	(59.6)	138.9	(57.6)
Other	3.0	(2.6)	2.9	(2.4)
Total	$157.5	$ (75.0)	$156.8	$ (72.5)
Unamortized intangibles:				
Trade names	47.4	—	47.2	—
Total intangibles	$204.9	$ (75.0)	$204.0	$ (72.5)

Amortization expense related to intangible assets for the first quarters ended March 31, 2018 and March 31, 2017 was $2.2 million and $2.1 million, respectively.

Amortization expense for each of the five succeeding years is projected as follows:

(In millions)	2018	2019	2020	2021	2022
	$8.8	$8.6	$8.5	$8.1	$7.9

The change in the carrying amount of goodwill by reporting segment for the three months ended March 31, 2018, is as follows:
(In millions)

	Water Systems	Fueling Systems	Distribution	Consolidated
Balance as of December 31, 2017	$139.3	$ 63.6	$ 33.9	$ 236.8
Acquisitions	—	—	1.5	1.5
Foreign currency translation	0.6	0.1	—	0.7
Balance as of March 31, 2018	$139.9	$ 63.7	$ 35.4	$ 239.0

8. EMPLOYEE BENEFIT PLANS

Defined Benefit Plans - As of March 31, 2018, the Company maintained two domestic pension plans and three German pension plans. The Company used a December 31, 2017 measurement date for these plans. One of the Company's domestic pension plans covers one active management employee, while the other domestic plan covers all eligible employees (plan was frozen as of December 31, 2011). The two domestic and three German plans collectively comprise the 'Pension Benefits' disclosure caption.

Other Benefits - The Company's other post-retirement benefit plan provides health and life insurance to domestic employees hired prior to 1992.

The following table sets forth the aggregated net periodic benefit cost for all pension plans for the first quarters ended March 31, 2018 and March 31, 2017:

(In millions)	Pension Benefits First Quarter Ended		Other Benefits First Quarter Ended	
	March 31, 2018	March 31, 2017	March 31, 2018	March 31, 2017
Service cost	$0.2	$ 0.1	$—	$ —
Interest cost	1.3	1.4	0.1	0.1
Expected return on assets	(2.1)	(2.2)	—	—
Amortization of:				
Prior service cost	—	—	—	0.1
Actuarial loss	0.7	0.6	0.1	—
Settlement cost	—	—	—	—
Net periodic benefit cost	$0.1	$ (0.1)	$0.2	$ 0.2

The Company adopted ASU 2017-07 in the first quarter ended March 31, 2018. The service cost component of net periodic benefit cost above is recorded in Selling, general, and administrative expenses within the Condensed Consolidated Statements of Income, while the remaining components are recorded to Other income/(expense), net. The prior year amounts have been reclassified to provide comparable presentation in line with the guidance.

In the first quarter ended March 31, 2018, the Company made contributions of $0.7 million to the funded plans. The amount of contributions to be made to the plans during the calendar year 2018 will be finalized by September 15, 2018, based upon the funding level requirements identified and year-end valuation performed at December 31, 2017.

9. INCOME TAXES

The Company’s effective tax rate from continuing operations for the three month period ended March 31, 2018 was negative 8.7 percent as compared to 1.3 percent for the three month period ended March 31, 2017. The effective tax rate is lower than the U.S. statutory rate of 21 percent primarily due to the recognition of the foreign-derived intangible income (FDII) provisions in the U.S. Tax Cuts and Jobs Act (Tax Act) and certain discrete events.

The decrease in the effective tax rate for the three months ended March 31, 2018, compared with the same period in 2017, was primarily affected by the Tax Act, which reduced the U.S. federal corporate income tax rate from 35 percent to 21 percent effective January 1, 2018. The Company also reflected an estimated tax benefit of $3.1 million associated with the FDII provisions of the Tax Act that were effective for the first time during 2018. In addition, during the three month period ended March 31, 2018, the Company released a valuation allowance of $5.4 million related to state NOLs and incentives as it is no longer in a three-year cumulative loss position for certain state income tax purposes.

The Company’s accounting for certain aspects of the Tax Act remains provisional. As noted at year-end 2017, the Company was able to reasonably estimate certain effects and, therefore, recorded provisional adjustments associated with the deemed repatriation transition tax and the remeasurement of deferred taxes. The Company has not made any additional measurement-period adjustments related to these items during the quarter as the analysis requires significant data from foreign subsidiaries that is not yet final due to future statutory deadlines as well as pending guidance from state and local tax authorities in the U.S. However, the Company is continuing to gather additional information to complete our accounting for these items. The accounting for the tax effects of the Tax Act will be completed in 2018.

10. DEBT

Debt consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
Prudential Agreement	$ 60.0	$ 60.0
Tax increment financing debt	20.3	20.8
New York Life	75.0	75.0
Credit Agreement	118.8	67.0
Capital leases	0.1	0.1
Foreign subsidiary debt	4.1	3.5
Less: unamortized debt issuance costs	(0.3)	(0.3)
	$ 278.0	$ 226.1
Less: current maturities	(152.9)	(100.5)
Long-term debt	$ 125.1	$ 125.6

Debt outstanding, excluding unamortized debt issuance costs, at March 31, 2018 matures as follows:

(In millions)	Total	Year 1	Year 2	Year 3	Year 4	Year 5	More Than 5 Years
Debt	$278.2	$152.9	$31.3	$1.2	$1.3	$1.3	$90.2
Capital leases	0.1	—	0.1	—	—	—	—
	$278.3	$152.9	$31.4	$1.2	$1.3	$1.3	$90.2

Prudential Agreement

The Company maintains the Third Amended and Restated Note Purchase and Private Shelf Agreement (the "Prudential Agreement") with an initial borrowing capacity of $250.0 million. The Prudential Agreement bears a coupon of 5.79 percent with a final maturity in 2019. Principal installments of $30.0 million are payable annually, including the date of maturity of April 30, 2019, with any unpaid balance due at that time. There is no additional borrowing capacity resulting from principal payments made by the Company. As of March 31, 2018, the Company has $100.0 million borrowing capacity available under the Prudential Agreement.

Project Bonds

The Company, Allen County, Indiana and certain institutional investors maintain a Bond Purchase and Loan Agreement. Under the agreement, Allen County, Indiana issued a series of Project Bonds entitled “Taxable Economic Development Bonds, Series 2012 (Franklin Electric Co., Inc. Project)." The aggregate principal amount of the Project Bonds that were issued, authenticated, and are now outstanding thereunder was limited to $25.0 million. These Project Notes ("Tax increment financing debt") bear interest at 3.6 percent per annum. Interest and principal balance of the Project Notes are due and payable by the Company directly to the institutional investors in aggregate semi-annual installments commencing on July 10, 2013, and concluding on January 10, 2033.

New York Life

The Company maintains an uncommitted and unsecured private shelf agreement with NYL Investors LLC, an affiliate of New York Life (the "New York Life Agreement"), entered into on May 27, 2015 for $150.0 million maximum aggregate principal borrowing capacity and authorized issuance of $75.0 million of floating rate senior notes due May 27, 2025. These senior notes have a floating interest rate of one-month USD LIBOR (1.88 percent as of March 31, 2018) plus a spread of 1.35 percent with interest-only payments due on a monthly basis. As of March 31, 2018, there was $75.0 million remaining borrowing capacity under the New York Life Agreement.

Credit Agreement

The Company maintains the Third Amended and Restated Credit Agreement (the "Credit Agreement”). The Credit Agreement has a maturity date of October 28, 2021 and commitment amount of $300.0 million. The Credit Agreement provides that the Borrowers may request an increase in the aggregate commitments by up to $150.0 million (not to exceed a total commitment of $450.0 million). Under the Credit Agreement, the Borrowers are required to pay certain fees, including a facility fee of 0.100% to 0.275% (depending on the Company's leverage ratio) of the aggregate commitment, which fee is payable quarterly in arrears. Loans may be made either at (i) a Eurocurrency rate based on LIBOR plus an applicable margin of 0.75% to 1.60% (depending on the Company's leverage ratio) or (ii) an alternative base rate as defined in the Credit Agreement.

As of March 31, 2018, the Company had $118.8 million in outstanding borrowings which were primarily used for acquisition and working capital needs, $5.3 million in letters of credit outstanding, and $175.9 million of available capacity under the Credit Agreement.

Covenants
The Company’s credit agreements contain customary financial covenants. The Company’s most significant agreements and restrictive covenants are in the New York Life Agreement, the Project Bonds, the Prudential Agreement, and the Credit Agreement; each containing both affirmative and negative covenants. The affirmative covenants relate to financial statements, notices of material events, conduct of business, inspection of property, maintenance of insurance, compliance with laws and most favored lender obligations. The negative covenants include limitations on loans, advances and investments, and the granting of liens by the Company or its subsidiaries, as well as prohibitions on certain consolidations, mergers, sales and transfers of assets. The covenants also include financial requirements including a maximum leverage ratio of 3.50 to 1.00 and a minimum interest coverage ratio of 3.00 to 1.00. Cross default is applicable with the Prudential Agreement, the Project Bonds, the New York Life Agreement, and the Credit Agreement but only if the Company is defaulting on an obligation exceeding $10.0 million. The Company was in compliance with all financial covenants as of March 31, 2018.

11. EARNINGS PER SHARE
The Company calculates basic and diluted earnings per common share using the two-class method. Under the two-class method, net earnings are allocated to each class of common stock and participating security as if all of the net earnings for the period had been distributed. The Company's participating securities consist of share-based payment awards that contain a nonforfeitable right to receive dividends and therefore are considered to participate in undistributed earnings with common shareholders.

Basic earnings per common share excludes dilution and is calculated by dividing net earnings allocable to common shares by the weighted-average number of common shares outstanding for the period. Diluted earnings per common share is calculated by dividing net earnings allocated to common shares by the weighted-average number of common shares outstanding for the period, as adjusted for the potential dilutive effect of non-participating share-based awards.

The following table sets forth the computation of basic and diluted earnings per share:

(In millions, except per share amounts)	First Quarter Ended March 31, 2018	March 31, 2017
Numerator:		
Net income attributable to Franklin Electric Co., Inc.	$21.2	$ 15.7
Less: Undistributed earnings allocated to participating securities	0.2	0.1
Less: Undistributed earnings allocated to redeemable noncontrolling interest	—	0.1
Net income available to common shareholders	$21.0	$ 15.5
Denominator:		
Basic weighted average common shares outstanding	46.6	46.4
Effect of dilutive securities:		
Non-participating employee stock options and performance awards	0.5	0.6
Diluted weighted average common shares outstanding	47.1	47.0
Basic earnings per share	$0.45	$ 0.33
Diluted earnings per share	$0.45	$ 0.33

There were 0.3 million and 0.2 million stock options outstanding for the first quarters ended March 31, 2018 and March 31, 2017, respectively, that were excluded from the computation of diluted earnings per share, as their inclusion would be anti-dilutive.

12. EQUITY ROLL FORWARD

The schedule below sets forth equity changes in the first quarter ended March 31, 2018:

(In thousands)	Common Stock	Additional Paid in Capital	Retained Earnings	Minimum Pension Liability	Cumulative Translation Adjustment	Noncontrolling Interest	Total Equity	Redeemable Noncontrolling Interest
Balance as of December 31, 2017	$4,663	$240,136	$604,905	$(49,364)	$(99,683)	$ 1,964	$702,621	$ 1,502
Net income			21,174			195	21,369	(154)
Dividends on common stock			(5,037)				(5,037)	
Common stock issued	3	639					642	
Common stock repurchased	(20)		(7,929)				(7,949)	
Share-based compensation	6	3,320					3,326	
Currency translation adjustment					6,943	40	6,983	12
Pension liability, net of tax				601			601	
Balance as of March 31, 2018	$4,652	$244,095	$613,113	$(48,763)	$(92,740)	$ 2,199	$722,556	$ 1,360

13. ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS)

Changes in accumulated other comprehensive income/(loss) by component for the first quarters ended March 31, 2018 and March 31, 2017, are summarized below:

(In millions)

For the first quarter ended March 31, 2018:	Foreign Currency Translation Adjustments	Pension and Post-Retirement Plan Benefit Adjustments (2)	Total
Balance as of December 31, 2017	$ (99.7)	$ (49.3)	$(149.0)
Other comprehensive income/(loss) before reclassifications	6.9	—	6.9
Amounts reclassified from accumulated other comprehensive income/(loss) (1)	—	0.6	0.6
Net other comprehensive income/(loss)	6.9	0.6	7.5
Balance as of March 31, 2018	$ (92.8)	$ (48.7)	$(141.5)
For the first quarter ended March 31, 2017			
Balance as of December 31, 2016	$ (118.4)	$ (51.5)	$(169.9)
Other comprehensive income/(loss) before reclassifications	8.4	—	8.4
Amounts reclassified from accumulated other comprehensive income/(loss) (1)	—	0.5	0.5
Net other comprehensive income/(loss)	8.4	0.5	8.9
Balance as of March 31, 2017	$ (110.0)	$ (51.0)	$(161.0)

(1) This accumulated other comprehensive income/(loss) component is included in the computation of net periodic pension cost (refer to Note 8 for additional details) and is included in the "Other income/(expense), net" line of the Company's condensed consolidated statements of income.

(2) Net of tax expense of $0.2 million and $0.3 million for the first quarters ended March 31, 2018 and March 31, 2017, respectively.

Amounts related to noncontrolling interests were not material.

14. SEGMENT AND GEOGRAPHIC INFORMATION
The accounting policies of the operating segments are the same as those described in Note 1 of the Company's Form 10-K. Revenue is recognized based on the invoice price at the point in time when the customer obtains control of the product, which is typically upon shipment to the customer. During the second quarter of 2017, as a result of acquisitions, the Company revised its reportable segments to include a Distribution segment. This change in reporting segments required the Company to realign its internal and external reporting. The Company retrospectively revised prior periods results to conform with current period presentations. There is no impact on the Company's previously reported consolidated financial position, results of operations, or cash flows. The Water and Fueling segments include manufacturing operations and supply certain components and finished goods, both between segments and to the Distribution segment. The Company accounts for intersegment revenue transactions consistent with independent third party transactions, that is, at current market prices. Operating income by segment is based on net sales less identifiable operating expenses and allocations and includes profits recorded on sales to other segments of the Company.

Financial information by reportable business segment is included in the following summary:

(In millions)	First Quarter Ended March 31, 2018	March 31, 2017
	Net sales	
Water Systems		
External sales		
United States & Canada	$80.8	$ 71.7
Latin America	29.1	33.0
Europe, Middle East & Africa	49.3	41.4
Asia Pacific	20.8	21.5
Intersegment sales		
United States & Canada	11.8	—
Total sales	191.8	167.6
Distribution		
External sales	—	—
United States & Canada	56.2	—
Intersegment sales	—	—
Total sales	56.2	—
Fueling Systems		
External sales	—	—
United States & Canada	32.8	29.5
All other	26.6	23.2
Intersegment sales	—	—
Total sales	59.4	52.7
Intersegment Eliminations/Other	(11.8)	—
Consolidated	$295.6	$ 220.3

First Quarter
Ended
March 31,
2018