

DONALDSON CO INC
Form 11-K
June 30, 2005

SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 11K

(Mark One)

- x ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT of 1934
(FEE REQUIRED) for the fiscal year ended December 31, 2004 or
- o TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT of 1934
(NO FEE REQUIRED) for the transition period from _____ to _____

Commission file number 1-7891

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

DONALDSON COMPANY, INC.
EMPLOYEE STOCK OWNERSHIP AND
RETIREMENT SAVINGS PLAN

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

DONALDSON COMPANY, INC.
1400 WEST 94TH STREET
MINNEAPOLIS, MINNESOTA 55431

**Donaldson Company, Inc.
Employee Stock Ownership
and Retirement Savings Plan**

(formerly known as the Donaldson Company, Inc.

Retirement Savings Plan)

**Financial Statements and Supplemental Schedule
December 31, 2004 and 2003**

**Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan**
(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)
Index

Page(s)

Report of Independent Registered Public Accounting Firm

1

Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan (formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

Financial Statements

| | |
|---|-----|
| Statement of Net Assets Available for Benefits December 31, 2004 and 2003 | 2 |
| Statement of Changes in Net Assets Available for Benefits Year Ended December 31, 2004 | 3 |
| Notes to Financial Statements | 4-8 |

Supplemental Schedule

| | |
|---|---|
| Schedule H, line 4i Schedule of Assets (Held at End of Year) December 31, 2004 | 9 |
|---|---|

Note: Other schedules required by 29 CFR 2520.103-10 of the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974 have been omitted because they are not applicable.

Report of Independent Registered Public Accounting Firm

To the Participants and Administrator of
Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan
(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

In our opinion, the accompanying statement of net assets available for benefits and the related statement of changes in net assets available for benefits present fairly, in all material respects, the net assets available for benefits of the Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan (formerly known as the Donaldson Company, Inc. Retirement Savings Plan) (the Plan) at December 31, 2004 and 2003, and the changes in net assets available for benefits for the year ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Plan's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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. An audit includes examining, on a test

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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. We believe that our audits provide a reasonable basis for our opinion.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedule referred to in the accompanying index is presented for the purpose of additional analysis and is not a required part of the basic financial statements, but is supplementary information required by the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. The supplemental schedule is the responsibility of the Plan's management. The supplemental schedule has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

As described in Note 1, effective June 30, 2004, the Donaldson Company, Inc. Employee Stock Ownership Plan was merged into the Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan. In connection with this merger, \$225,904,864 was transferred into the Plan.

/s/ PricewaterhouseCoopers LLP
 Minneapolis, Minnesota
 June 29, 2005

1

Donaldson Company, Inc.

Employee Stock Ownership and Retirement Savings Plan

(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

Statement of Net Assets Available for Benefits

December 31, 2004 and 2003

| | 2004 | 2003 |
|---|-------------|-------------|
| Assets | | |
| Investments, at fair value | | |
| Interest-bearing cash | \$ 32,343 | \$ 32,343 |
| Mutual funds | 158,390,204 | 135,017,301 |
| Donaldson Company, Inc. common stock fund | 289,708,528 | 49,223,743 |
| Participant loans | 3,716,347 | 3,185,225 |
| | 451,815,079 | 187,458,612 |
| Total investments, at fair value | | |
| Receivables | | |
| Investment income receivable | | 400 |
| | 451,815,079 | 187,459,012 |
| Liabilities | | |
| Investment settlements payable | | 2,687 |

| | <u>2004</u> | <u>2003</u> |
|-----------------------------------|----------------|----------------|
| Net assets available for benefits | \$ 451,815,079 | \$ 187,456,325 |

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

2

Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan
(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)
Statement of Changes in Net Assets Available for Benefits
Year Ended December 31, 2004

Investment income

| | |
|---|-------------------|
| Interest and dividend income | \$ 5,954,144 |
| Net appreciation of the fair value of investments | 38,375,769 |
| | <u>44,329,913</u> |

Contributions

| | |
|--------------|-------------------|
| Employer | 2,318,107 |
| Participants | 14,273,380 |
| | <u>16,591,487</u> |

Deductions

| | |
|-------------------------------|--------------|
| Benefits paid to participants | (23,067,591) |
|-------------------------------|--------------|

| | |
|---|----------------|
| Administrative expenses | (24,396) |
| | <hr/> |
| | (23,091,987) |
| | <hr/> |
| Transfers | |
| Transfer from ultrafilter, Inc. 401(k) Plan | 421,120 |
| Transfer from MSCA, LLC 401(k) Plan | 203,357 |
| Transfer from Donaldson Company, Inc. Employee Stock Ownership Plan | 225,904,864 |
| | <hr/> |
| Net increase in net assets available for benefits | 264,358,754 |
| Net assets available for benefits | |
| Beginning of year | 187,456,325 |
| | <hr/> |
| End of year | \$ 451,815,079 |
| | <hr/> |

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

Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan
(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)
Notes to Financial Statements
December 31, 2004 and 2003

1. Description of Plan

The Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan (formerly known as the Donaldson Company, Inc. Retirement Savings Plan) (the Plan) is a contributory defined contribution plan sponsored by Donaldson Company, Inc. (the Company). The Plan is subject to the applicable provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

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The following description of the Plan is provided for general information purposes only. Participants should refer to the summary plan description for a more complete description of the Plan's provisions.

Fidelity Management Trust Company is the Plan's trustee (the Trustee) and recordkeeper.

Effective June 30, 2004, the Donaldson Company, Inc. Employee Stock Ownership Plan was merged into the Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan (formerly known as the Donaldson Company, Inc. Retirement Savings Plan). Assets of the Donaldson Company, Inc. Employee Stock Ownership Plan totaling \$225,904,864 were transferred into the Plan.

Effective April 1, 2004, the ultrafilter, Inc. 401(k) Plan and the MSCA, LLC 401(k) Plan were merged into the Donaldson Company, Inc. Retirement Savings Plan. The ultrafilter, Inc. 401(k) Plan covered employees of ultrafilter, Inc., which was acquired by Donaldson Company, Inc. on April 7, 2003. The MSCA, LLC 401(k) Plan covered employees of MSCA, LLC, which became 100% owned by Donaldson Company, Inc. on November 2, 2002. The assets transferred into the Donaldson Company, Inc. Retirement Savings Plan were \$421,120 for the ultrafilter, Inc. 401(k) Plan and \$203,357 for the MSCA, LLC 401(k) Plan.

Eligibility

All regular full-time and part-time employees are eligible to participate in the Plan upon employment, as defined by the Plan document. Employees covered by a labor agreement are not eligible for any Company contributions.

Contributions

Each year, eligible participants may contribute to the Plan up to 25% of pre-tax annual compensation, as defined by the Plan. Participants may also contribute amounts representing rollover distributions from other qualified retirement plans with the approval of the Administrative Committee.

Under the terms of the Plan, the Company makes fixed matching contribution and could make discretionary contributions to the Plan. Company contributions were made in cash or through submission of shares of common stock of the Company. Any cash contributions were invested directly in common stock of the Company.

4

Donaldson Company, Inc. Employee Stock Ownership and Retirement Savings Plan

(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

Notes to Financial Statements

December 31, 2004 and 2003

The Company made matching fixed contributions to the Plan based on participant contributions into the Plan. Fixed matching contributions were calculated at 100% of up to 3% of compensation deferred by the participant and deposited into the Plan and 50% of the next 2% of compensation deferred by participants and deposited into the Plan.

The Company may make discretionary contributions to the Plan from time to time. Discretionary contributions are allocated among the participants pro rata based upon total annual compensation of participants who have 1,000 hours of service in the Plan year and are in employment of the Company on the last day of the Plan year. Subsequent to each Plan year ended, the Company made a discretionary contribution of \$1,095,996 and \$972,906 for the Plan years ended December 31, 2004 and 2003, respectively.

Participant Accounts

Participants direct the investment of their contributions into various investment options offered by the Plan. If a participant does not allocate their contributions, the contributions are placed in the Fidelity Managed Income Portfolio II Fund. Company contributions are allocated in Donaldson Company, Inc. stock.

The allocation of the participant's contributions to the investment funds may be changed daily. There are no restrictions on transfers among or between the various investment options for employee contributions. Each participant's account is credited with his or her contributions, including rollover distributions, and his or her share of Company contributions, and an allocation of related investment earnings thereon. Allocation of investment earnings is based on the value of the participant's account at the close of each day. Participants can transfer Company contributions after they have five years of service.

Vesting

Participants are 100% vested in their accounts at all times.

Payment of Benefits

Upon termination of employment, disability or termination of the Plan, a participant or designated beneficiary will receive the vested portion of the participant's account balance in a lump-sum payment. Hardship withdrawals, as defined in the Plan document, are allowed at any time, subject to approval by the Plan.

Participant Loans

Under the Plan document, participants may borrow up to 50% of their account balance or \$50,000, whichever is less. Loans must be repaid by the participant within five years, unless the loan is used to acquire the participant's primary residence in which case the term may not exceed ten years. The loan interest is one percent over the prime lending rate on the last business day of the month preceding the month in which the loan is granted. Interest rates on outstanding loans at December 31, 2004, ranged from 5% to 5.25%. Loans mature at various dates through December 2011 and are generally paid through monthly payroll deductions.

Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan
(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)
Notes to Financial Statements
December 31, 2004 and 2003

Plan Termination

The Company has the right under the Plan agreement to amend or terminate the Plan. In the event of termination of the Plan, the assets of the Plan will be distributed to the participants in accordance with the Plan document.

2. Summary of Significant Accounting Policies

The accompanying financial statements have been prepared on an accrual basis. The following is a summary of significant policies which are in conformity with accounting principles generally accepted in the United States of America and are consistently followed by the Plan in the preparation of its financial statements.

Valuation of Investments

Investments in mutual funds are stated at fair value based on quoted market prices. Investments in the Donaldson Company, Inc. Common Stock Fund are valued based on the fair value of the underlying investments, primarily Donaldson Company, Inc. common stock, which is valued at quoted market prices. Participant loans are valued at estimated fair value, which consists of outstanding principal and any related accrued interest.

Investment Earnings

Investment income is recorded as earned. Dividend income is recorded on the ex-dividend date. The Plan presents the net appreciation (depreciation) in the fair value of its investments in the Statement of Changes in Net Assets Available for Benefits. Net appreciation

(depreciation) consists of the realized gains or losses and the unrealized appreciation (depreciation) on those investments.

Contributions

Participant contributions and Company matching contributions are recorded in the period the employer makes the payroll deductions. Employer discretionary contributions, if any, are recorded in the period they are contributed to the Plan, which is after the end of the Plan year.

Benefits Paid to Participants

Benefits paid to participants are recorded when paid.

Plan Expenses

Investment management fees and administrative fees charged by the Trustee are paid by the Plan. All other expenses are paid by the Company, including legal, accounting and other services.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of net assets available for benefits at the date of the financial statements and the reported amounts of changes in net assets available for benefits during the reporting period. Ultimate results could differ from those estimates.

**Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan**

(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

Notes to Financial Statements

December 31, 2004 and 2003

Risks and Uncertainties

The Plan provides for various investment options in various combinations of investment securities. Investment securities are exposed to various risk factors including, but not limited to, interest rates, market conditions and credit risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the Statement of Net Assets Available for Benefits in future periods.

Concentration of Market Risk

At December 31, 2004 and 2003, approximately 64% and 26% of the Plan's net assets were invested in the Donaldson Company, Inc. common stock, respectively. The underlying value of this fund is dependent on the performance of Donaldson Company, Inc. and the market's evaluation of such performance. It is at least reasonably possible that changes in the fair value of Donaldson Company, Inc. common stock in the near term could materially affect participants' account balances and the amounts reported in the Statement of Net Assets Available for Benefits and the Statement of Changes in Net Assets Available for Benefits.

3. Investments

The current value of individual investments that represent 5% or more of the Plan's net assets is as follows:

| | 2004 | 2003 |
|--------------------------------------|----------------|---------------|
| Donaldson Company, Inc. common stock | \$ 289,708,528 | \$ 49,223,743 |

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| | 2004 | 2003 |
|---|----------------|----------------|
| Fidelity Managed Income Portfolio II Fund | 40,488,086 | 39,448,813 |
| Fidelity Equity Income Fund | 37,126,275 | 34,570,063 |
| Fidelity Magellan Fund | 19,316,241 | 18,338,352 |
| Fidelity Contrafund | 19,906,124 | 16,304,415 |
| Schroeder U.S. Opportunities Fund | 10,638,564 | |
| All other investments individually less than 5% | 34,631,261 | 29,573,226 |
| | \$ 451,815,079 | \$ 187,458,612 |

During the year ended December 31, 2004, investments had net appreciation value as follows:

| | |
|--------------------------------------|---------------|
| Mutual funds | \$ 8,952,883 |
| Donaldson Company, Inc. common stock | 29,422,886 |
| | \$ 38,375,769 |

At December 31, 2004, Donaldson Company, Inc. common stock consists of 8,876,099 shares of the Company's common stock valued at \$289,183,312 and \$525,216 of cash in the Fidelity Institutional Cash Portfolio. At December 31, 2003, Donaldson Company, Inc. common stock consists of 822,184 shares of the Company's common stock valued at \$48,640,405 and \$583,338 of cash in the Fidelity Institutional Cash Portfolio.

Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan
 (formerly known as the Donaldson Company, Inc. Retirement Savings Plan)
Notes to Financial Statements
December 31, 2004 and 2003

4. Tax Status

The Plan has received a favorable determination letter from the Internal Revenue Service, dated October 20, 1995, stating that the Plan is designed in accordance with the applicable sections of the Internal Revenue Code (the "Code") and is therefore generally exempt from federal income taxes under provisions of Section 501(a). The Plan has been amended since receiving the determination letter. However, the Plan administrator believes that the Plan is currently designed and being operated in compliance with the applicable requirements of the Code. Therefore, no provision for income taxes has been included in the Plan's financial statements.

5. Related Party Transactions

Participants have the option to direct their contributions to be invested in mutual funds which are sponsored by the Trustee, and a Company stock fund comprised primarily of Donaldson Company, Inc. common stock. The Trustee is authorized, under contract provisions and by exemption under 29 CFR 408(b) of ERISA regulations, to invest in securities under its control and in the Company. For the year ended December 31, 2004, purchases and sales of securities of the Company were \$41,937,686 and \$54,777,061, respectively.

SUPPLEMENTAL SCHEDULE

Donaldson Company, Inc.
Employee Stock Ownership and Retirement Savings Plan

(formerly known as the Donaldson Company, Inc. Retirement Savings Plan)

Schedule H, line 4i Schedule of Assets (Held at End of Year)

December 31, 2004

EIN 41-0222640

Plan Number 007

Schedule I

| (a) | (b) | (c) | (d) | (e) |
|-----|--|---|----------------|------------------|
| | Identity of Issue, Borrower, Lessor or Similar Party | Description of Investment Including the Maturity Date, Rate of Interest, Collateral, Par or Maturity Value | Cost** | Current Value |
| * | Donaldson Company, Inc. | Common Stock, 8,876,099 shares | \$ 289,183,312 | |
| * | Fidelity Institutional Cash Portfolio | Money Market Fund | | 525,216 |
| * | Fidelity Managed Income Portfolio II Fund | Mutual Fund, 40,488,064 units of participation | | 40,488,086 |
| * | Fidelity Equity Income Fund | Mutual Fund, 703,416 units of participation | | 37,126,275 |
| * | Fidelity Magellan Fund | Mutual Fund, 186,109 units of participation | | 19,316,241 |
| * | Fidelity Contrafund | Mutual Fund, 350,831 units of participation | | 19,906,124 |
| * | Fidelity Divers International Fund | Mutual Fund, 295,958 units of participation | | 8,476,231 |
| * | Fidelity Balanced Fund | Mutual Fund, 453,525 units of participation | | 8,081,816 |
| | Schroeder U.S. Opportunities Fund | Mutual Fund, 551,507 units of participation | | 10,638,564 |
| | Spartan US Equity Index Fund | Mutual Fund, 126,312 units of participation | | 5,413,752 |
| | Sterling Small Cap Value I Fund | Mutual Fund, 184,169 units of participation | | 3,431,060 |
| | PIMCO Total Return Fund | Mutual Fund, 320,420 units of participation | | 3,418,880 |
| | Brokeragelink Fund | Mutual Fund, 1,200,305 units of participation | | 1,200,305 |
| | Turner Concentrated Growth Institutional Fund | Mutual Fund, 78,562 units of participation | | 524,007 |
| | FMI KB Emerging Growth Fund | Mutual Fund, 36,521 units of participation | | 368,863 |
| * | Participants | Participant loans receivable, interest rates from 5% to 5.25%, payable through December 2011 | | 3,716,347 |
| | | | | \$ 451,815,079 |

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* Denotes party-in-interest.

** Historical cost information is omitted as it is not required by the Department of Labor under the instructions to the Form 5500 for participant directed accounts.

9

Pursuant to the requirements of the Securities Exchange Act of 1934, the trustees (or other persons who administer the employee benefit plan) have duly caused this annual report to be signed on its behalf by the undersigned thereunto duly authorized.

DONALDSON COMPANY, INC. EMPLOYEE
STOCK OWNERSHIP AND RETIREMENT SAVINGS
PLAN

(Name of Plan)

Date June 30, 2005

By: Donaldson Company, Inc., the Plan
Administrator

/s/ Thomas R. VerHage

Thomas R. VerHage
Vice President, Chief Financial Officer

EXHIBIT INDEX

ANNUAL REPORT ON FORM 11-K

Exhibit 23 Consent of Independent Public Accountants