ARDEN REALTY INC
Form 10-K
March 16, 2006

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934.**

For the fiscal year ended December 31, 2005

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OR 1934.**

For the transition period from ___to ___

Commission File Number 1-12193

ARDEN REALTY, INC.

(Exact name of registrant as specified in its charter)

Maryland	**95-4578533**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

11601 Wilshire Boulevard, 4th Floor
Los Angeles, California 90025-1740
(Address and zip code of principal executive offices)
Registrant s telephone number, including area code: (310) 966-2600
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.01 par value	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

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

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

Indicate by checkmark 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. þ Yes o 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. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. (Check one):

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

The aggregate market value of the shares of common stock held by non-affiliates was approximately $2.4 billion based on the closing price on the New York Stock Exchange for such shares on June 30, 2005.

The number of the Registrant s shares of common stock outstanding was 67,331,215 as of March 15, 2006.

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PART I

Forward-Looking Statements

This Form 10-K, including the documents incorporated herein by reference, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, pertaining to, among other things, our future results of operations, cash available for distribution, acquisitions, lease renewals, property development, property renovation, capital requirements and general business, industry and economic conditions applicable to us. Also, documents we subsequently file with the Securities and Exchange Commission, or SEC, and incorporated herein by reference will contain forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of the risk factors set forth below and the matters set forth or incorporated in this Form 10-K generally. We caution you, however, that this list of factors may not be exhaustive, particularly with respect to future filings.

ITEM 1. *BUSINESS*

(a) GENERAL

The terms Arden Realty , us , we and our as used in this report refer to Arden Realty, Inc. We were incorporated in Maryland in May 1996 and completed our initial public offering in October 1996. Commencing with our taxable year ended December 31, 1996, we have operated and qualified as a real estate investment trust, or REIT, for federal income tax purposes. We are a self-administered and self-managed REIT that owns, manages, leases, develops, renovates and acquires commercial properties located in Southern California. We are the sole general partner of Arden Realty Limited Partnership, or the Operating Partnership, and as of December 31, 2005, we owned approximately 97.5% of the Operating Partnership s common partnership units. We conduct substantially all of our operations through the Operating Partnership and its consolidated subsidiaries.

(b) INDUSTRY SEGMENTS

We are currently involved primarily in one industry segment, the operation of commercial real estate located in Southern California. The financial information contained in this report relates primarily to this industry segment.

(c) DESCRIPTION OF BUSINESS

We are a full-service real estate organization managed by 6 senior executive officers who have experience in the real estate industry ranging from 15 to 36 years and who collectively have an average of 21 years of experience. We perform all property management, construction management, accounting, finance and acquisition and disposition activities and a majority of our leasing transactions for our portfolio with our staff of approximately 300 employees.

As of December 31, 2005, we were Southern California s largest publicly traded office landlord as measured by total net rentable square feet owned. As of December 31, 2005, our portfolio of primarily suburban office properties consisted of 116 properties and 192 buildings containing approximately 18.5 million net rentable square feet and our operating portfolio was 91.9% occupied.

Proposed Merger

On December 21, 2005, we, along with Arden Realty Limited Partnership, our operating partnership, and Atlas Partnership Merger Sub, Inc., referred to throughout as the partnership merger sub, a wholly-owned subsidiary of ours, entered into a definitive Agreement and Plan of Merger, referred to throughout as the merger agreement, with General Electric Capital Corporation, also referred to as GECC, Atlas Merger Sub, Inc., referred to as REIT merger sub, a wholly-owned subsidiary of GECC, Trizec Properties, Inc., and Trizec Holdings Operating LLC. Pursuant to the merger agreement, GECC will acquire us and our subsidiaries through a series of transactions including the merger of our company into the REIT Merger Sub, referred to as the REIT merger, as well as a merger of the Partnership Merger Sub into our operating partnership, referred to as the partnership merger.

In the REIT merger, we will be merged with and into REIT merger sub, with REIT merger sub surviving, and shares of our common stock converted into the right to receive merger consideration of $45.25, plus an amount equal to a prorated portion of our normal $0.505 quarterly dividend. In the partnership merger, partnership merger sub will be merged with and into our operating partnership, and holders of our OP units, subject to certain eligibility requirements, may elect to either participate in the redemption and exchange of OP units for class B units of Trizec Holdings Operating LLC, plus an amount equal to a prorated portion of our $0.505 quarterly distribution, or have their

OP units converted into the right to receive merger consideration of $45.25, plus an amount equal to a prorated portion of our $0.505 quarterly distribution.

In connection with the mergers, we will sell to Trizec Operating Company a portfolio of certain of our properties, comprised of 13 office properties totaling 4.1 million square feet, certain undeveloped land parcels and other assets. Following the

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consummation of the transactions, GECC or its affiliates will own or control the entity or entities which will succeed to the ownership of the remaining properties owned by us.

Our board has unanimously approved the merger agreement and has recommended it for approval by our common stockholders. The parties expect to close the transaction in the second quarter of 2006. The closing of the merger is subject to, among other things, a number of customary conditions, including the approval by the affirmative vote of two-thirds of the holders of shares of our common stock. The transaction is not subject to any financing condition.

Portfolio Management

We perform all portfolio management activities, including on-site property management, management of all lease negotiations, construction management of tenant improvements or tenant build-outs, property renovations and capital expenditures for our portfolio. We directly manage these activities from approximately 48 management offices located throughout our portfolio. The activities of these management offices are supervised by four regional offices with oversight by our corporate office to ensure consistent application of our operating policies and procedures. Each regional office is strategically located within the Southern California submarkets where our properties are located and is managed by a regional First Vice President who is responsible for supervising the day-to-day activities of our management offices. Each regional office is staffed with leasing, property management, building engineering, construction and information systems specialists, referred to as our Regional Service Teams. By maintaining a regionally focused organizational structure led by seasoned managers, we are able to quickly respond to our tenants needs and market opportunities.

All of our management and regional offices are networked with our corporate office and have access to the Internet and our e-mail, accounting and lease management systems. Our accounting and lease management systems employ the latest technology and allow both corporate and field personnel access to tenant and prospective tenant-related information to enhance responsiveness and communication of marketing and leasing activity for each property.

We currently lease approximately 59% of our portfolio s net rentable space using our in-house staff. We employ outside brokers who are monitored by our Regional Service Teams for the remainder of our net rentable space. Our in-house leasing program allows us to closely monitor rental rates and lease terms for new and renewal leases and reduce third-party leasing commissions.

Business Strategies

Our primary business strategy is to actively manage our portfolio to achieve gains in rental rates and occupancy, control operating expenses and maximize income from ancillary operations and services. When market conditions permit, we may also selectively develop, renovate or acquire new properties in submarkets that add value and fit strategically into our portfolio. We may also sell existing properties and use the net proceeds to repay outstanding indebtedness or place such proceeds into investments that we believe will generate higher long-term value.

Through our corporate and regional offices, we implement our business strategies by:

- using integrated decision making to provide proactive solutions to the space needs of tenants in the markets where we have extensive real estate expertise and relationships;

- emphasizing quality service, tenant satisfaction and retention; · employing intensive property marketing and leasing programs; and

- implementing cost control management techniques and systems that capitalize on economies of scale and concentration arising from the size and geographic focus of our portfolio and our technical expertise in reducing energy consumption expenses.

We believe the implementation of these operating practices has been instrumental in maximizing the operating results of our portfolio.

Integrated Decision Making

We use a multidisciplinary approach to our decision making by having our regional management, leasing, construction management, acquisition, disposition and finance teams coordinate their activities to enhance responsiveness to market opportunities and to provide proactive solutions to the space needs of tenants in the submarkets where we have extensive real estate and technical expertise. This integrated approach permits us to analyze the specific requirements of existing and prospective tenants and the economic terms and costs for each transaction on a timely and efficient basis. We are therefore able to commit to leasing, development, acquisition or disposition terms quickly, which facilitates an efficient completion of lease negotiation and tenant build-out, shorter vacancy periods after lease expirations and the timely completion of development, acquisition or disposition transactions.

Quality Service and Tenant Satisfaction

We strive to provide quality service through our multidisciplinary operating approach resulting in timely responses to our tenants needs. Our seasoned Regional Service Teams interact and resolve issues relating to tenant satisfaction and day-to-day operations. For portfolio-wide operational and administrative functions, our corporate office provides support to all regional offices and provides immediate response for critical operational issues. We believe providing quality service leads to enhanced tenant retention.

Proactive Marketing and Leasing

The concentration of many of our properties within particular office submarkets and our relationships with a broad array of businesses and outside brokers enables us to pursue proactive marketing and leasing strategies, to effectively monitor the demand for office space in our existing submarkets, to efficiently identify the office space requirements of existing and prospective tenants and to offer tenants a variety of space alternatives across our portfolio.

Cost Control and Operating Efficiencies

The size and geographic focus of our portfolio provides us with the opportunity to enhance portfolio value by controlling operating costs. We seek to capitalize on the economies of scale and concentration which result from the geographic focus of our portfolio through the ownership and management of multiple properties within particular submarkets compared to the maintenance of standardized processes and systems for cost control at each of our properties. These cost controls and operating efficiencies allowed us to achieve a 66.4% ratio of property operating results to total property revenues in 2005.

Operating Strategies

Based on our geographic focus in Southern California, experience in the local real estate markets and our evaluation of current market conditions, we believe the following key factors provide us with opportunities to maximize returns:

- the broad diversification and balance of the Southern California economy and our tenant base minimizes our dependence on any one industry segment or limited group of tenants;

- the relative resiliency of the Southern California real estate market, as measured by lower vacancy rates compared to the national average and flat or increasing rental rates in our key submarkets compared to the average decreases in rates reported for the nation since the beginning of the office real estate sector downturn in 2001; and

- the limited construction of new office properties in the Southern California region due to substantial building construction limitations and a minimal amount of developable land in many key submarkets.

Internal Operating Strategy

Our internal operating strategy seeks growth by:

- stabilizing occupancy throughout our portfolio and by increasing rental rates, as market conditions permit;

- maintaining or increasing the retention rate of expiring leases;

- capitalizing on economies of scale and concentration due to the size and geographic focus of our portfolio;

- controlling operating expenses through active cost control management techniques and systems; and

- sourcing new and innovative revenue streams while providing high quality services to our tenants.

Stabilizing Occupancy and Increasing Rental Rates

Various published reports noted that Southern California achieved approximately 10.5 million square feet of positive net absorption in 2005 with average rental rates increasing approximately 6.5%. Our in-house leasing teams, working with outside leasing brokers, continuously monitor each submarket to identify prospective tenants who are in need of new or additional space and to obtain the most favorable lease terms. We also strive to achieve growth in rental revenues by negotiating annual or mid-term increases in rental rates in a majority of our leases.

Retaining Existing Tenants

We also seek to retain our existing tenants when leases expire. Retention of existing tenants reduces the costs of lease rollover by eliminating the down-time required to find a replacement tenant and reducing build-out costs required for new tenants. We believe that we have been successful in attracting and retaining a diverse tenant base by actively managing our properties with an emphasis on tenant satisfaction and retention. During 2005, we retained approximately 67% of our leases prior to lease expiration.

Capitalizing on Economies of Scale and Concentration

In order to capitalize on economies of scale and concentration arising from the size and geographic focus of our portfolio, each of our Regional Service Teams is responsible for several properties, which spreads administrative and maintenance costs over those properties and reduces per square foot expenses. In addition, contracting in bulk for parking operations, construction materials, building services and supplies on a portfolio-wide basis also reduces our overall operating expenses.

Cost Control Management Techniques and Systems

We strive to control our operating expenses through active management at all of our properties. We continuously monitor the operating performance of our properties and employ bulk or competitive purchasing techniques, energy-enhancing and expense recovery technologies when appropriate. These system enhancements include:

- lighting retrofits;
- replacement of inefficient heating, ventilation and air conditioning systems;
- computer-driven energy management systems that monitor and react to the climatic requirements of individual properties;
- automated and roving security systems that allow us to provide security services to our tenants at a lower cost;
- online competitive bid purchasing of supplies, building materials and construction services;
- enhancement of billing systems, which enables us to more efficiently recover operating expenses from our tenants; and
- on-going preventive maintenance programs to operate our building systems efficiently, thereby reducing operating costs.

Sourcing Additional Revenue While Providing High Quality Services to Tenants

We have invested in energy enhancement programs within our portfolio with the aim of reducing energy consumption, enhancing efficiency and lowering operating costs. We have also participated in the Environmental Protection Agency s, or the EPA, Energy Star Program. This program involves top commercial real estate landlords throughout the United States and rigorous bench-marking procedures that track individual building energy efficiencies. Currently, of the 881 total Energy Star designated office buildings awarded nationally during 2005, 291were awarded in California; of those, we had 58 EPA Energy Star Certified buildings in our portfolio.

We have a taxable REIT subsidiary, next>edge, that markets our expertise in energy solutions and facilities management. next>edge now assists companies outside of our portfolio in increasing their energy efficiency and reducing costs by employing the latest technologies and the most energy-efficient operational strategies developed to date. These technologies include lighting, heating, ventilation and air conditioning retrofits, energy management system installations, and on-site power generation such as cogeneration projects and solar photovoltaic systems.

External Operating Strategy

We believe in the diversity and balance of the Southern California economy and the commercial real estate market. We have a management team that has extensive experience and knowledge in this market which we believe provides us with a competitive advantage in identifying and capitalizing on selective development, renovation, acquisition and disposition opportunities.

Subject to capital availability and market conditions, our approach has been to seek development, renovation and acquisition opportunities in markets where we have an existing presence and where the following conditions exist:

low vacancy rates;

opportunities for rising rents due to employment growth and population movements;

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- a minimal amount of developable land; and
- significant barriers to entry due to constraints on new development, including strict entitlement processes, height and density restrictions or other governmental requirements.

Competition

We compete with other owners of office properties to attract tenants to our properties, to acquire new properties and to obtain suitable land for development. Ownership of competing properties is currently diversified among many different types, from publicly traded companies and institutional investors, including other REITs, to small enterprises and individual owners. No one owner or group of owners currently dominate or significantly influence the markets in which we operate. See Risk Factors Competition affects occupancy levels, rents and the cost of land which could adversely affect our revenues.

California Electric Utility Deregulation

Problems associated with deregulation of the electric industry in California have resulted in significantly higher costs in some areas over the past few seasons. All of our properties are currently located in areas served by utilities that either produce their own electricity, or that have procured long-term, fixed-rate contracts with commercial electrical providers.

Approximately 22% of our properties and 16% of the total rentable square footage of our portfolio are subject to leases that require our tenants to pay all utility costs and the remainder provide that our tenants will reimburse us for utility costs in excess of a base year amount. See Risk Factors Rising energy costs and power outages in California may have an adverse effect on our operations and revenue.

Employees

As of December 31, 2005, we had approximately 300 full-time employees that perform all of our property and construction management, accounting, finance, acquisition and disposition activities and a majority of our leasing transactions.

Available Information

We file with the SEC our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K (and all amendments to those reports), proxy statements and registration statements. The public may read and copy any materials we file with the SEC at the SEC s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may also obtain public information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an internet site at www.sec.gov that contains reports, proxy and information regarding registrants, including us, that file electronically. This annual report on Form 10-K and other periodic and current reports, and amendments to those reports, filed or furnished with the SEC, are also available, free of charge, by viewing the SEC filings available in the Investor Information section of our website at www.ardenrealty.com as soon as reasonably practicable after we file or furnish them with the SEC.

(d) FOREIGN OPERATIONS

We do not engage in any foreign operations or derive any revenue from foreign sources.

ITEM 1A. *RISK FACTORS*

In addition to the other information contained or incorporated by reference in this Form 10-K, readers should carefully consider the following risk factors.

Risks Related to the Proposed Merger

On December 21, 2005, we, entered into a merger agreement with GECC and Trizec pursuant to which GECC will acquire us through the process set forth under the heading Proposed Merger in Item 1 above. In connection with the proposed merger, we have filed a definitive proxy statement with the SEC. The proxy statement contains important information about us, the proposed merger and other related matters. We urge all of our stockholders to read the proxy statement. In relation to the proposed merger, we are subject to certain risks including, but not limited to, those set forth below.

Failure to complete the merger could negatively impact our stock price and our future business and financial results.

Completion of the proposed merger is subject to the satisfaction or waiver of various conditions, including the receipt of approval from our stockholders, receipt of various approvals and authorizations, and the absence of any order, injunction or decree preventing the completion of the proposed merger. There is no assurance that all of the various conditions will be satisfied or waived.

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If the proposed merger is not completed for any reason, we will be subject to several risks, including the following:

being required, under certain circumstances, including if we sign a definitive agreement with respect to a superior proposal from another potential buyer, to pay a termination fee of $100.0 million;

being required, under certain circumstances, including if we breach the merger agreement, to reimburse GECC for up to $10.0 million of its costs and expenses in connection with the merger agreement;

having incurred certain costs relating to the proposed merger that are payable whether or not the merger is completed, including legal, accounting, financial advisor and printing fees; and

having had the focus of management directed toward the proposed merger and integration planning instead of on our core business and other opportunities that could have been beneficial to us.

In addition, we would not realize any of the expected benefits of having completed the proposed merger. If the proposed merger is not completed, we cannot assure our stockholders that these risks will not materialize or materially adversely affect our business, financial results, financial condition and stock price.

Provisions of the merger agreement may deter alternative business combinations and could negatively impact our stock price if the merger agreement is terminated in certain circumstances.

Restrictions in the merger agreement on solicitation generally prohibit us from soliciting any acquisition proposal or offer for a merger or business combination with any other party, including a proposal that might be advantageous to our stockholders when compared to the terms and conditions of the proposed merger. If the merger is not completed, we may not be able to conclude another merger, sale or combination on as favorable terms, in a timely manner, or at all. If the merger agreement is terminated, we, in certain specified circumstances, may be required to pay a termination fee of up to $100.0 million to GECC. In addition, under certain circumstances, we may be required to pay GECC an expense fee of $10.0 million. These provisions may deter third parties from proposing or pursuing alternative business combinations that might result in greater value to our stockholders than the merger.

Our stock price and businesses may be adversely affected if the merger is not completed.

If the merger is not completed, the trading price of our common stock may decline, to the extent that the current market prices reflect a market assumption that the merger will be completed. In addition, our businesses and operations may be harmed to the extent that tenants, vendors and others believe that we cannot effectively operate in the marketplace on a stand-alone basis, or there is tenant or employee uncertainty surrounding the future direction of the strategy of our company on a stand-alone basis.

Uncertainty regarding the merger may cause tenants, vendors and others to delay or defer decisions concerning their business with our company, which may harm our results of operations going forward if the merger is not completed.

Because the merger is subject to several closing conditions, including the approval of the merger by our stockholders, uncertainty exists regarding the completion of the merger. This uncertainty may cause tenants, vendors and others to delay or defer decisions concerning their business with our company, which could negatively affect our business and results of operations.

If the planned merger were not completed, we could suffer a number of consequences that may adversely affect our business, results of operations and stock price, including the following:

activities relating to the merger and related uncertainties may lead to a loss of revenue that we may not be able to regain if the merger does not occur;

the market price of our common stock could decline following an announcement that the merger has been abandoned, to the extent that the current market price reflects a market assumption that the merger will be completed;

we would remain liable for our costs related to the merger, such as legal fees and a portion of the investment banking fees;

we may not be able to continue our present level of operations and therefore would have to scale back our present level of business and consider additional reductions; and

we may not be able to take advantage of alternative business opportunities or effectively respond to competitive pressures.

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Real Estate Investment Risks

An inability to retain tenants or rent space upon lease expirations may adversely affect our revenues and our ability to service our debt.

Through 2010, 2,667 leases, including month-to-month leases, comprising approximately 75% of our leased net rentable square footage and approximately 72% of our annualized base rents at December 31, 2005 are scheduled to expire as follows:

Year	Number of Leases Expiring	Percentage of Aggregate Portfolio Leased Square Feet	Percentage of Aggregate Portfolio Annualized Base Rent
Month-to-Month	135	2.1%	1.8%
2006	593	14.0%	13.4%
2007	576	14.3%	13.4%
2008	593	17.4%	17.2%
2009	395	13.1%	12.6%
2010	375	14.3%	13.9%

If we are unable to promptly renew or relet leases for all or a substantial portion of this space, or if the rent upon renewal or reletting are significantly lower than expected, our cash flow and business could be adversely affected which would limit our ability to service our debt.

Lack of non-farm job growth in Southern California or a deterioration of the local and national economy will adversely affect our operating results.

All of our properties are located in Southern California. In 2005, the Southern California economy experienced a 1.3% increase in job growth representing approximately 86,000 non-farm jobs. We believe non-farm job growth to be a leading indicator of office demand for the region. During 2006, a total of approximately 2.8 million square feet of occupied space, representing approximately 16.0% of our total net rentable space, including month-to-month leases, will expire. Negative non-farm job growth in our submarkets or a deterioration of the local and/or national economy may result in a decline in occupancy and rental rates and may cause tenant concessions to increase and would most likely negatively affect our operating performance and property values.

Competition affects occupancy levels, rents and cost of land which could adversely affect our revenues.

Many office properties compete with our properties in attracting tenants to lease space. Some of the competing properties may be newer, better located or owned by parties better capitalized than we are. Although ownership of these competing properties is currently diversified among many different types of owners, from publicly traded companies and institutional investors to small enterprises and individual owners, and no one or group of owners currently dominate or significantly influence the market, consolidation of owners could create efficiencies and marketing advantages for the consolidated group that could adversely affect us. These competitive advantages, the number of competitors and the number of competitive commercial properties in a particular area could have a material adverse effect on the rents we can charge, our ability to lease space in our existing properties or at newly acquired or developed properties and the prices we have to pay for developable land.

The financial condition and solvency of our tenants may reduce our cash flow.

Tenants may experience a downturn in their business which may cause them to miss rental payments when due or to seek the protection of bankruptcy laws, which could result in rejection and termination of their leases or a delay in recovering possession of their premises. Although we have not experienced material losses from tenant bankruptcies, we cannot assure you that tenants will not file for bankruptcy protection in the future or, if any tenants file, that they will affirm their leases and continue to make rental payments in a timely manner.

Because real estate investments are illiquid, we may not be able to sell properties when appropriate.

Equity real estate investments are relatively illiquid. That illiquidity may tend to limit our ability to sell properties promptly in response to changes in economic or other conditions. In addition, the Internal Revenue Code of 1986, as amended, may under specified circumstances impose a 100% prohibited transaction tax on the profits derived from our sale of properties held for fewer than four years, which could affect our ability to sell our properties.

Rising energy costs and power outages in California may have an adverse effect on our operations and revenue.

Problems associated with deregulation of the electric industry in California have resulted in significantly higher costs in some areas. All of our properties are currently located in areas served by utilities that either produce their own electricity, or that have procured long-term, fixed rate contracts with commercial electrical providers. While we have no information suggesting that any future service interruptions are expected, we believe that higher utility costs may continue as price increases are allowed by the California Public Utility Commission or other regulatory agencies.

Approximately 22% of our buildings and 16% of the total rentable square footage of our portfolio are subject to leases that require our tenants to pay all utility costs. The remainder of our leases provide that tenants will reimburse us for utility costs in excess of a base year amount.

Although we have not experienced any material losses resulting from electric deregulation, it is possible that some or all of our tenants will not fulfill their lease obligations and reimburse us for their share of any significant electric rate increases and that we will not be able to retain or replace our tenants if energy problems in California continue.

Increases in taxes and regulatory compliance costs may reduce our revenue.

Except for our triple net leases, we may not be able to pass all real estate tax increases through to some or all of our tenants. Therefore, any tax increases may adversely affect our cash flow and our ability to pay or refinance our debt obligations. Our properties are also subject to various federal, California and local regulatory requirements, such as requirements of the Americans with Disabilities Act, and California and local fire and life safety requirements. Failure to comply with these requirements could result in the imposition of fines by governmental authorities or awards of damages to private litigants. We believe that our properties are currently in substantial compliance with these regulatory requirements. We cannot assure you, however, that these requirements will not be changed or that new requirements will not be imposed that would require significant unanticipated expenditures by us and could have an adverse effect on our cash flow, the amounts available for distributions and on our business.

We may acquire properties through partnerships or joint ventures with third parties that could result in financial dependency and management conflicts.

We may participate with other entities in property ownership through joint ventures or partnerships in the future. Depending on the characteristics and business objectives of the joint venture or partnership, we may not have voting control over the joint venture or partnership. Partnership or joint venture investments may, under certain circumstances, involve risks not otherwise present, including:

- our partners or co-venturers might become bankrupt;
- our partners or co-venturers might at any time have economic or other business interests or goals which are inconsistent with our business interests or goals; and
- our partners or co-venturers may be in a position to take action contrary to our instructions or requests contrary to our policies or objectives.

Neither the partnership agreement of our operating partnership nor our governing documents prevent us from participating in joint ventures with our affiliates. Because a joint venture with an affiliate may not be negotiated in a traditional arm s length transaction, terms of the joint venture may not be as favorable to us as we could obtain if we entered into a joint venture with an outside third party.

We may not be able to successfully integrate or finance our acquisitions.

As we acquire additional properties, we will be subject to risks associated with managing new properties, including building systems not operating as expected, delay in or failure to lease vacant space and tenants failing to renew leases as they expire. In addition, our ability to manage our growth effectively will require us to successfully integrate our new acquisitions into our existing accounting systems and property management structure. We cannot assure you that we will be able to succeed with that integration or effectively manage additional properties or that newly acquired properties will perform as expected. Changing market conditions, including competition from other purchasers of suburban office properties, may diminish our opportunities for attractive additional acquisitions. Moreover, acquisition costs of a property may exceed original estimates, possibly making the property uneconomical.

Our acquisitions and renovations may not perform as expected.

Although we currently have no plans to significantly expand or renovate our properties, we may do so in the future, subject to certain restrictions contained in the merger agreement. Expansion and renovation projects may inconvenience and displace existing tenants, require us to engage in time consuming up-front planning and engineering activities and expend capital, and require us to obtain various government and other approvals, the receipt of which cannot be assured. While our policies with respect to expansion and renovation activities are intended to limit some of the risks otherwise associated with these activities, we will nevertheless incur risks, including expenditures of funds on, and devotion of our time to, projects that may not be completed.

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Our development activities may be more expensive than anticipated and may not yield our anticipated results.

We have preliminary architectural designs completed for an additional 475,000 net rentable square feet at the Howard Hughes Center in Los Angeles, California and have completed preliminary designs on a build-to-suit office building at our Long Beach Airport Business Park. We have entitlements for up to 600 hotel rooms at the Howard Hughes Center. We also have a 5-acre developable land parcel in Torrance, California that we are also marketing for a build-to-suit building. Certain restrictions contained in the merger agreement limit our ability to move forward on these developments without the approval of GECC. We also intend to review, from time to time, other opportunities for developing and constructing office buildings and other commercial properties in accordance with our development and underwriting policies.

We expect to finance our development activities over the next 24 months, subject to certain restrictions contained in the merger agreement, through net cash provided by operating activities, proceeds from asset sales, proceeds from our lines of credit or other secured borrowings.

Risks associated with our development activities may include:

- abandonment of development opportunities due to a lack of financing or other reasons;

- construction costs of a property exceeding original estimates, possibly making the property uneconomical;

- occupancy rates and rents at a newly completed property may not be sufficient to make the property profitable;

- construction and lease-up may not be completed on schedule, resulting in increased debt service expense and construction costs; and

- development activities would also be subject to risks relating to the inability to obtain, or delays in obtaining, all necessary zoning, land-use, building, occupancy and other required governmental permits and authorizations.

We are not subject to any limit on the amount or percentage of our assets that may be invested in any single property or any single geographic area.

Our governing documents do not restrict the amount or percentage of our assets that we may invest in a single property or geographic area. All of our properties are currently in Southern California and we have no immediate plans to invest outside of Southern California. Although the overall Southern California economy is diverse and well balanced, the geographic concentration of our portfolio may make us more susceptible to changes affecting the Southern California economy and real estate markets or damages from regional events such as earthquakes.

We may not be able to expand into new markets successfully.

While our business is currently limited to the Southern California market, it is possible that we will in the future expand our business to new geographic markets. We will not initially possess the same level of familiarity with new markets outside of Southern California, which could adversely affect our ability to manage, lease, develop or acquire properties in new localities.

Financing Risks

Our amount of debt could limit our operational flexibility or otherwise adversely affect our financial condition.

As of December 31, 2005, we had total debt of approximately $1.6 billion, consisting of approximately $419.6 million in secured debt and approximately $1.2 billion of unsecured debt. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

Our indebtedness could:

- require us to dedicate a substantial portion of our cash flow to pay our debt, thereby reducing the availability of our cash flow to fund distributions, working capital, capital expenditures, acquisition and development activity and other business purposes;

- make it more difficult for us to satisfy our debt obligations;

limit our ability to refinance our debt and obtain additional debt financing; and

increase our vulnerability to general adverse economic and real estate industry conditions and limit our flexibility in planning for, or reacting to, changes in our business and the real estate industry.

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Despite current indebtedness levels, we may still be able to incur substantially more debt in the future, which would increase the risks associated with our substantial leverage. Neither the partnership agreement of our operating partnership nor our governing documents limit the amount or the percentage of indebtedness that we may incur. We may borrow up to a maximum of $330 million under our two lines of credit. As of December 31, 2005, we had the ability to borrow an additional $70.5 million under these two lines of credit. If new debt is added to our current debt levels, the related risks that we now face could intensify and could increase the risk of default on our indebtedness.

Scheduled debt payments could adversely affect our financial condition.

Our cash flow could be insufficient to meet required payments of principal and interest when due. In addition, we may not be able to refinance existing indebtedness, which in virtually all cases requires substantial principal payments at maturity, and, if we can refinance, the terms of the refinancing might not be as favorable as the terms of our existing indebtedness. If principal payments cannot be refinanced, extended or paid with proceeds of other capital transactions, such as new equity capital, our cash flow will not be sufficient in all years to repay all maturing debt and continue to service and repay our debt obligations.

Rises in interest rates could adversely affect our financial condition.

An increase in prevailing interest rates would have an immediate effect on the interest rates charged on our variable rate debt which rise and fall upon changes in interest rates. At December 31, 2005, approximately 14% of our debt was variable rate debt. Increases in interest rates would also impact the refinancing of our fixed rate debt. If interest rates are higher when our fixed debt becomes due, we may be forced to borrow at the higher rates. If prevailing interest rates or other factors result in higher interest rates, the increased interest expense would adversely affect our cash flow and our ability to service our debt. As a protection against rising interest rates, we may enter into agreements such as interest rate hedges, caps, floors and other interest rate exchange contracts. These agreements, however, increase our risks as to the other parties to the agreements not performing or that the agreements could be unenforceable.

Many of our properties are subject to mortgage financing which could result in foreclosure if we are unable to pay or refinance the mortgages when due.

We currently have four outstanding mortgage financings totaling approximately $358.2 million that are secured by 46 of our properties. The properties in each of these financings are fully cross-collateralized and cross-defaulted. To the extent two or more mortgages are cross-defaulted, a default in one mortgage will trigger a default in the other mortgages. The cross-defaults can give the lender a number of remedies depending on the circumstances such as the right to increase the interest rate, demand additional collateral, accelerate the maturity date of the mortgages or foreclose on and sell the properties. To the extent two or more mortgages are cross-collateralized, a default in one mortgage will allow the mortgage lender to foreclose upon and sell the properties that are not the primary collateral for the loan in default. Three additional properties are subject to single property mortgages totaling approximately $61.5 million at December 31, 2005. If we are unable to meet our obligations under these mortgages, we could be forced to pay higher interest rates or provide additional collateral or the properties subject to the mortgages could be foreclosed upon and sold, which could have a material adverse effect on us and our ability to pay or refinance our debt obligations.

Tax Risks

Our desire to qualify as a REIT restricts our ability to accumulate cash that might be used in future periods to make debt payments or to fund future growth.

In order to qualify as a REIT and avoid federal income tax liability, we must distribute to our stockholders at least 90% of our net taxable income, excluding net capital gain, and to avoid income taxation, our distributions must not be less than 100% of our net taxable income, including capital gains. To avoid excise tax liability, our distributions to our stockholders for the year must exceed the sum of 85% of its ordinary income, 95% of its capital gain net income, and any undistributed taxable income from prior years. As a result of these distribution requirements, we do not expect to accumulate significant amounts of cash. Accordingly, these distributions could significantly reduce the cash available to us in subsequent periods to make payments on our debt obligations and to fund future growth.

Our operating partnership intends to qualify as a partnership, but we cannot guarantee that it will qualify.

Our operating partnership intends to qualify as a partnership for federal income tax purposes. However, if our operating partnership were a publicly traded partnership, it would be treated as a corporation instead of a partnership for federal income tax purposes unless at least 90% of its income is qualifying income as defined in the Internal Revenue Code. The income requirements applicable to REITs and the definition of qualifying income for purposes of this 90% test are similar in most respects. Qualifying income for the 90% test generally includes passive income, such as specified types of real property rents, dividends and interest. We believe that our operating partnership would meet this 90% test, but we cannot guarantee that it would. If our operating partnership were to be taxed as a corporation, it would incur substantial tax liabilities and we would fail to qualify as a REIT for federal income tax purposes.

We may suffer adverse tax consequences and be unable to attract capital if we fail to qualify as a REIT.

We believe that since our taxable year ended December 31, 1996, we have been organized and operated, and intend to continue to operate, so as to qualify for taxation as a REIT under the Internal Revenue Code. Although we believe that we have been and will continue to be organized and have operated and will continue to operate so as to qualify for taxation as a REIT, we cannot assure you that we have been or will continue to be organized or operated in a manner so as to qualify or remain so qualified. For us to qualify as a REIT, we must satisfy numerous requirements established under highly technical and complex Internal Revenue Code provisions for which there are only limited judicial and administrative interpretations and tests regarding various factual matters and circumstances not entirely within our control. The complexity of these provisions and of the applicable Treasury Regulations that have been promulgated under the Internal Revenue Code is greater in the case of a REIT, like us, that holds its assets through an investment in a partnership. No assurance can be given that legislation, new regulations, administrative interpretations or court decisions will not significantly change the tax laws with respect to our qualification as a REIT or the federal income tax consequences of qualification. We are, however, not aware of any pending legislation that would adversely affect our ability to qualify as a REIT. Our qualification and taxation as a REIT depends on our ability to meet, through actual annual operating results, asset diversification, distribution levels and diversity of stock ownership, the various qualification tests imposed under the Internal Revenue Code, the results of which have not been and will not be reviewed by our tax counsel.

If we failed to qualify as a REIT in any taxable year, we would be subject to federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. Moreover, unless entitled to relief under specific statutory provisions, we also would be disqualified as a REIT for the four taxable years following the year during which qualification was lost. If we were disqualified as a REIT, our ability to raise additional capital could be significantly impaired. This could reduce the funds we would have available to pay distributions to our stockholders and to service our debt.

Even if we qualify for and maintain our REIT status, we will be subject to certain federal, state and local taxes on our income and property. For example, if we have net income from a prohibited transaction, specifically sales or other taxable dispositions of property held primarily for sale to customers in the ordinary course of business, that income will be subject to a 100% tax.

Other Risks

We are subject to agreements and policies that may deter change in control offers that might be attractive to our stockholders.

Certain provisions of our charter and bylaws may delay, defer or prevent a third party from making offers to acquire us or assume control over us. For example, such provisions may:

- deter tender offers for our common stock, which offers may be attractive to the stockholders; and

- deter purchases of large blocks of common stock, thereby limiting the opportunity for stockholders to receive a premium for their common stock over then-prevailing market prices.

Our charter contains a provision designed to prevent a concentration of ownership among our stockholders that would cause us to fail to qualify as a REIT. Under the Internal Revenue Code, not more than 50% in value of our outstanding shares of common stock may be owned, actually or constructively, by five or fewer individuals, including specific kinds of entities, at any time during the last half of our taxable year. In addition, if we, or an owner of 10% or more of our common stock, actually or constructively owns 10% or more of a tenant of ours, or a tenant of any partnership in which we are a partner, the rent received by us from that tenant will not be qualifying income for purposes of the REIT gross income tests. In order to protect us against the risk of losing REIT status, the ownership limit included in our charter limits actual or constructive ownership of our outstanding shares of common stock by any single stockholder to 9.0%, by value or by number of shares, whichever is more restrictive, of the then outstanding shares of common stock. Actual or constructive ownership of shares of common stock in excess of the ownership limit will cause the violative transfer or ownership to be void with respect to the transferee or owner as to that number of shares in excess of the ownership limit and such shares will be automatically transferred to a trust for the exclusive benefit of one or more qualified charitable organizations. That transferee or owner will have no right to vote such shares or be entitled to dividends or other distributions with respect to such shares.

Although our Board of Directors presently has no intention of doing so, except as described below, our Board of Directors could waive this restriction with respect to a particular stockholder if it were satisfied, based upon the advice of counsel or a ruling from the Internal Revenue Service, that ownership by such stockholder in excess of the ownership limit would not jeopardize our status as a REIT and our Board of Directors otherwise decided such action would be in our best interests. Our Board of Directors has waived our ownership limit with respect to Mr. Ziman, our Chairman and CEO, and certain family members and affiliates and has permitted these parties to actually and constructively own up to 13.0% of the outstanding shares of common stock.

Our charter authorizes our Board of Directors to cause us to issue authorized but unissued shares of common stock or preferred stock and to reclassify any unissued shares of common stock or classify any unissued and reclassify any previously classified but unissued shares of preferred stock and, with respect to the preferred stock, to set the preferences, rights and other terms of such classified or unclassified shares. Although our Board of Directors has no such intention at the present time, it could establish a series of preferred stock that could, depending on the terms of such series, delay, defer or prevent a transaction or a change in control that might involve a premium price for the common stock or otherwise be in the best interest of our stockholders.

Our Board of Directors is divided into three classes of directors. Directors of each class are chosen for three-year terms upon the expiration of their current terms and each year one class of directors will be elected by the stockholders. The staggered terms of directors may reduce the possibility of a tender offer or an attempt to change control even though a tender offer or change in control might be in the best interest of our stockholders.

Losses in excess of our insurance coverage or uninsured losses could adversely affect our cash flow.

We carry comprehensive liability, fire, extended coverage, terrorism and rental loss insurance policies which currently cover all of our properties with specifications and insured limits that we believe are adequate and appropriate under the circumstances. Some losses, however, are generally not insured against because it is not economically feasible to do so. Should an uninsured loss or a loss in excess of insured limits occur, we could lose our capital invested in the property, as well as the anticipated future revenue from the property and, in the case of debt which is recourse to us, we would remain obligated for any mortgage debt or other financial obligations related to the property. Any loss would adversely affect our cash flow with respect to the property subject to the loss. Moreover, we would generally be liable for any unsatisfied obligations other than non-recourse obligations with respect to the property subject to the loss.

Lack of availability of insurance coverage for biological, chemical or nuclear terrorist attacks could adversely affect our financial condition.

Our current terrorism insurance policy, which has been extended to March 2007, specifically excludes biological, chemical or nuclear terrorist acts. We have been notified by our insurance broker that in the aftermath of the September 11th attacks, insurance carriers will continue to exclude these types of attacks from terrorism insurance policies or offer coverage for biological, chemical or nuclear attacks coverages at prohibitive costs. Although we did not derive more than 3.5% of our 2005 net operating income from any one of the properties in our portfolio, a biological, chemical or nuclear terrorist attack damaging several of our properties or negatively impacting the financial condition of our tenants could materially deteriorate our operating results and overall financial condition.

An earthquake could adversely affect our business.

All of our properties are located in Southern California, which is a high risk geographical area for earthquakes. Depending upon its magnitude, an earthquake could severely damage our properties which would adversely affect our business. We maintain earthquake insurance for our properties and the resulting business interruption. We cannot assure you that our insurance will be sufficient if there is a major earthquake.

Our properties may be subject to environmental liabilities.

Under federal, state and local environmental laws, a current or previous owner or operator of real estate may be required to investigate and clean up hazardous or toxic substances or petroleum product releases at the property and may be held liable to a governmental entity or to third parties for property damage and for investigation and clean-up costs in connection with the contamination. These laws typically impose clean-up responsibility and liability without regard to whether the owner knew of or caused the presence of the contaminants, and the liability under these laws has been interpreted to be joint and several unless the harm is divisible and there is a reasonable basis for allocation of responsibility. These costs may be substantial, and the presence of these substances, or the failure to remediate the contamination on the property, may adversely affect the owner s ability to sell or rent the property or to borrow against the property. Finally, third parties may have claims against the owner of the site based on damages and costs resulting from environmental contamination emanating from that site.

Specific federal, state and local laws, regulations and ordinances govern the removal, encapsulation or disturbance of asbestos-containing materials when those materials are in poor condition or in the event of construction, remodeling, renovation or demolition of a building. These laws may impose liability for release of asbestos-containing material and may provide for third parties to seek recovery from owners or operators of real properties for personal injury associated with asbestos-containing materials. In connection with the ownership and operation of our properties, we may be potentially liable for those costs.

In the past few years, independent environmental consultants have conducted or updated Phase I environmental assessments and other environmental investigations as appropriate at some of our properties. The environmental site assessments and investigations have identified 38 properties in our portfolio, representing approximately 43% of the total rentable square feet in the portfolio, affected by environmental concerns. These environmental concerns include properties that may be impacted by known or suspected (a) contamination caused by third party sources or (b) soil and/or groundwater contamination which has been remediated, and (c) those containing underground storage tanks or asbestos.

Of these properties, four are believed to be affected by contamination caused by third party sources and two of these also house an underground storage tank, two contain friable asbestos, twenty contain non-friable asbestos, and twelve house underground storage tanks only. The properties affected by contamination are primarily affected by petroleum and solvent substances, and in each case a third party has indemnified us for any and all problems associated with this contamination. With regard to those properties affected by asbestos, asbestos does not pose a health hazard if it is not disturbed in such a way to cause an airborne release of asbestos. Asbestos is friable when it can be crumbled, pulverized or reduced to powder by hand pressure, and non-friable when hand pressure cannot release encapsulated asbestos fibers. Friable asbestos is more likely to be released into the air than non-friable asbestos. We manage all asbestos in ways that minimize its potential to become airborne or otherwise threaten human health. Regarding underground storage tanks, subsurface leakage of the materials contained within the tank constitutes the primary risk posed by these devices. Of the fourteen underground storage tanks, two are currently being removed and no known UST-related regulatory violations or outstanding compliance issues exist with the remainder. We have also implemented a program to ensure appropriate double-wall construction, testing protocols, placement of tanks within bermed areas, and the installation of leak and spill detection equipment at relevant sites.

Environmental site assessments and investigations completed to date have not, however, revealed any environmental liability that we believe would have a material adverse effect on our business, assets or results of operations taken as a whole, nor are we aware of any material environmental liability. Nevertheless, it is possible that our environmental site assessments do not reveal all environmental liabilities or that there are material environmental liabilities of which we are unaware.

We believe that our properties are in compliance in all material respects with all federal, state and local laws regarding hazardous or toxic substances or petroleum products, except as noted above. We have not been notified by any governmental authority, and are not otherwise aware, of any material noncompliance, liability or claim relating to hazardous or toxic substances or petroleum products in connection with any of our present properties, other than as noted above. It is possible that future laws will impose material environmental liabilities on us and that the current environmental condition of our properties will be affected by tenants, by the condition of land or operations in the vicinity of our properties, such as the presence of underground storage tanks, or by third parties unrelated to us.

We may incur increased costs as a result of enacted and proposed changes in laws and regulations.

Enacted and proposed changes in the law and regulations affecting public companies, including the provisions of the Sarbanes-Oxley Act of 2002 and rules proposed by the SEC and by the New York Stock Exchange has resulted in significant increased compliance costs to us as we evaluate the implications of any new rules and comply to their requirements. The new rules could make it more difficult or more costly for us to obtain certain types of insurance, including director and officer liability insurance, and we may be forced to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. The impact of these events could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers. The compliance with and the provisions of the Sarbanes-Oxley Act in future years will result in significant continuing costs to us.

ITEM 1B. ***UNRESOLVED STAFF COMMENTS***

None.

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ITEM 2. ***PROPERTIES***

Existing Portfolio

As of December 31, 2005, our portfolio consists of 116 primarily office properties containing approximately 18.5 million net rentable square feet, which individually range from approximately 12,000 to 600,000 net rentable square feet. Of the 116 properties currently in service in our portfolio, 115, or 99%, are office properties. All of our properties are located in Southern California and most are in suburban areas in close proximity to main thoroughfares. We believe that our properties are located within desirable and established business communities and are well maintained. Our properties offer an array of amenities including high-speed internet access, security, parking, conference facilities, on-site management, food services and health clubs.

Following is a summary of our property portfolio as of December 31, 2005:

Location	**Number of Properties**			**Number of Buildings**	**Approximate Net Rentable Square Feet**	**Property Operating Results[1],[2] For the Year Ended December 31, 2005 ($000 s and unaudited)**
	Total	% of Total	&nont style="DISPLAY: inline; FONT-SIZE: 10pt; FONT-FAMILY: times new roman">	26,536		
Employee Compensation and Benefits	17,934	23,334				
Income Taxes Payable	2,542	3,154				
Other Current Liabilities	36,869	50,189				
Total Current Liabilities	87,081	107,159				
Long-Term Liabilities:						
Long-Term Debt	87,634	91,393				
Employee-Related Benefits	28,494	29,059				
Deferred Income Taxes, Long-Term Portion	9,435	11,671				
Other Liabilities	7,328	7,418				
Total Long-Term Liabilities	132,891	139,541				
Total Liabilities	219,972	246,700				
Shareholders' Equity:						
Preferred Stock, $0.02 par value; 1,000,000 shares authorized; no shares issued or outstanding	-	-				
	6,984	6,857				

Common Stock, $0.375 par value; 60,000,000 shares authorized; 18,622,921 and 18,284,746 shares issued and outstanding, respectively		
Additional Paid-In Capital	6,566	6,649
Retained Earnings	182,299	223,692
Accumulated Other Comprehensive Income (Loss)	(29,015)	(26,391)
Receivable from ESOP	(1,150)	(903)
Total Shareholders' Equity	165,684	209,904
Total Liabilities and Shareholders' Equity	$ 385,656	$ 456,604

See accompanying Notes to Condensed Consolidated Financial Statements.

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TENNANT COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(In thousands)

	Three Months Ended March 31	
	2009	2008
OPERATING ACTIVITIES		
Net Earnings (Loss)	$ (41,746)	$ 5,235
Adjustments to Net Earnings (Loss) to Arrive at Operating Cash Flow:		
Depreciation	5,356	4,307
Amortization	639	458
Deferred Tax Expense (Benefit)	595	420
Goodwill Impairment Charge	43,363	-
Stock-Based Compensation Expense	286	555
ESOP Income	(27)	(204)
Tax Benefit on ESOP	3	9
Allowance for Doubtful Accounts and Returns	166	233
Other, Net	1,376	843
Changes in Operating Assets and Liabilities, Excluding the Impact of Acquisitions:		
Accounts Receivable	21,149	(696)
Inventories	(2,536)	(5,966)
Accounts Payable	1,945	(6,096)
Employee Compensation and Benefits and Other Accrued Expenses	(15,456)	(9,938)
Income Taxes Payable/Prepaid	(2,300)	400
Other Assets and Liabilities	(1,640)	4,553
Net Cash Provided by (Used for) Operating Activities	11,173	(5,887)
INVESTING ACTIVITIES		
Purchases of Property, Plant and Equipment	(3,824)	(7,408)
Proceeds from Disposals of Property, Plant and Equipment	263	-
Acquisition of Businesses, Net of Cash Acquired	(2,295)	(81,365)
Net Cash Flows Provided by (Used for) Investing Activities	(5,856)	(88,773)
FINANCING ACTIVITIES		
Payments on Capital Leases	(1,092)	(786)
Change in Short-Term Debt, Net	(1)	4,795
Payment of Long-Term Debt	(10,006)	-
Issuance of Long-Term Debt	6,000	87,500
Purchases of Common Stock	-	(3,593)
Proceeds from Issuance of Common Stock	-	808
Tax Benefit on Stock Plans	(147)	232
Dividends Paid	(2,381)	(2,409)
Net Cash Flows Provided by (Used for) Financing Activities	(7,627)	86,547
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(276)	312
Net Increase (Decrease) in Cash and Cash Equivalents	(2,586)	(7,801)
Cash and Cash Equivalents at Beginning of Period	29,285	33,092
Cash and Cash Equivalents at End of Period	$ 26,699	$ 25,291
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash Paid During the Year for:		

Income Taxes	$	1,128	$	758
Interest	$	367	$	378
Supplemental Non-cash Investing and Financing Activities:				
Capital Expenditures Funded Through Capital Leases	$	1,360	$	571
Collateralized Borrowings Incurred for Operating Lease Equipment	$	1,968	$	782

See accompanying Notes to Condensed Consolidated Financial Statements.

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TENNANT COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
(in thousands, except shares and per share data)

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with the Securities and Exchange Commission ("SEC") requirements for interim reporting, which allows certain footnotes and other financial information normally required by accounting principles generally accepted in the United States of America to be condensed or omitted. In our opinion, the Condensed Consolidated Financial Statements contain all adjustments (consisting of only normal recurring adjustments) necessary for the fair presentation of our financial position and results of our operations. These statements should be read in conjunction with the Consolidated Financial Statements and Notes included in our Annual Report on Form 10-K for the year ended December 31, 2008. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year.

2. Newly Adopted Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard No. 157, "Fair Value Measurements" ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosure about fair value measurements. In February 2008, the FASB issued FASB Staff Position ("FSP") FAS 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements that Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13" ("FSP FAS 157-1"), which states that SFAS No. 157 does not address fair value measurements for purposes of lease classification or measurement. FSP FAS 157-1 does not apply to assets acquired and liabilities assumed in a business combination that are required to be measured at fair value under SFAS No. 141, "Business Combinations" ("SFAS No. 141"), or SFAS No. 141 (revised 2007) ("SFAS No. 141(R)"), regardless of whether those assets and liabilities are related to leases. In February 2008, the FASB also issued FSP FAS 157-2, "Effective date of FASB Statement No. 157" ("FSP FAS 157-2"). FSP FAS 157-2 defers the implementation of SFAS No. 157 for certain nonfinancial assets and liabilities. We adopted the required provisions of SFAS No. 157 as of January 1, 2008 and adopted the provisions of FSP FAS 157-2 on January 1, 2009. The adoptions of SFAS No. 157 and FSP FAS 157-2 did not have an impact on our financial position or results of operations.

In December 2007, the FASB issued SFAS No. 141(R). SFAS No. 141(R) requires most identifiable assets, liabilities, noncontrolling interests and goodwill acquired to be recorded at full fair value. This statement also establishes disclosure requirements that will enable users to evaluate the nature and financial effects of the business combination. The requirements are effective for fiscal years beginning on or after December 15, 2008. The adoption of SFAS No. 141(R) applies prospectively to business combinations completed on or after January 1, 2009. The adoption of SFAS No. 141(R) did not have a material impact on our financial position or results of operations as of January 1, 2009.

In April 2008, the FASB issued FSP FAS 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP FAS 142-3"), which amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, "Goodwill and Other Intangible Assets." FSP FAS 142-3 is effective for fiscal years beginning on or after December 15, 2008 and should be applied prospectively to intangible assets acquired after the effective date. The adoption of FSP FAS 142-3 did not have an impact on our financial position or results of operations.

In April 2009, the FASB issued FSP No. 141(R)-1, "Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arises from Contingencies" ("FSP No. 141(R)-1"), which amends and clarifies SFAS No. 141(R) to address application issues raised by preparers, auditors and members of the legal profession on initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. The requirements are effective for fiscal years beginning on or after December 15, 2008. The adoption of SFAS No. 141(R) will apply prospectively to business combinations completed on or after January 1, 2009. The adoption of FSP No. 141(R)-1 did not have an impact on our financial position or results of operations as of January 1, 2009.

3. Management Actions

2008 Actions – During the fourth quarter of 2008, we announced a workforce reduction program to reduce our worldwide employee base by approximately 8%, or about 240 people. A pretax charge of $14,551, including other associated costs of $290, was recognized in the fourth quarter of 2008 as a result of this program. The workforce reduction was accomplished primarily through the elimination of salaried positions across the organization. The pretax charge consisted primarily of severance and outplacement services and was included within Selling and Administrative Expense in the 2008 Consolidated Statement of Earnings.

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TENNANT COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
(in thousands, except shares and per share data)

A reconciliation of the beginning and ending liability balances is as follows:

	Severance, Early Retirement and Related Costs
2008 workforce reduction action	$ 14,261
Cash payments	(355)
Foreign currency adjustments	5
Balance as of December 31, 2008	13,911
Cash payments	(6,390)
Foreign currency adjustments	(318)
Adjustment of accrual	(1,328)
Balance as of March 31, 2009	$ 5,875

The $1,328 adjustment to the accrual balance during the first quarter of 2009 was primarily due to lower than anticipated severance costs in Europe both on an employee settlement basis and also the opportunity to eliminate open positions due to employee turnover thereby avoiding some severance payments.

4. Acquisitions and Divestitures

Acquisitions

On February 27, 2009, we acquired certain assets of Applied Cleansing Solutions Pty Ltd ("Applied Cleansing"), a long-term importer and distributor for Green Machines™ products in Australia and New Zealand, in a business combination for an initial purchase price of $556 in cash. This acquisition provides us with the opportunity to accelerate our growth in the city cleaning business within the Asia Pacific region. The purchase agreement also provides for additional contingent consideration to be paid for each of the four quarters following the acquisition date if certain future revenue targets are met. We have recorded additional contingent consideration of approximately $160.

Our February 27, 2009 acquisition of Applied Cleansing is accounted for as a business combination and the results of operations have been included in the Condensed Consolidated Financial Statements since the date of acquisition. The purchase price allocation is preliminary and will be adjusted based upon the final determination of fair value of assets acquired and liabilities assumed.

On December 1, 2008, we entered into an asset purchase agreement with Hewlett Equipment (“Hewlett”) for a purchase price of $625 in cash. The assets purchased consist of industrial equipment. Hewlett has been a distributor and service agent for Tennant Industrial and Commercial Equipment in Queensland, Australia since 1980. The purchase of Hewlett’s existing rental fleet of industrial equipment will accelerate Tennant’s strategy to grow its direct sales and service business in the key economic area of Australia. Hewlett will continue as a distributor and service agent of Tennant’s commercial equipment.

On August 15, 2008, we acquired Shanghai ShenTan Mechanical and Electrical Equipment Co. Ltd. (“Shanghai ShenTan”) for a purchase price including transaction costs of $598 in cash. The acquisition of Shanghai ShenTan, a 12 year exclusive distributor of Tennant products in Shanghai, China, will accelerate Tennant’s strategy to grow its direct sales and service business in the key economic area of Shanghai. The purchase agreement also provides for additional contingent consideration to be paid in each of the three one-year periods following the acquisition date if certain future revenue targets are met and if other future events occur. We anticipate that any amount paid under this earn-out would be considered additional purchase price. The earn-out is denominated in foreign currency which approximates $600 in the aggregate and is to be calculated based on 1) growth in revenues and 2) visits to specified customer locations during each of the three one-year periods following the acquisition date.

On March 28, 2008, we acquired Sociedade Alfa Ltda. ("Alfa") for an initial purchase price including transaction costs of $12,252 in cash and $1,445 in debt assumed. Alfa manufactures the Alfa brand of commercial cleaning machines, is based in Sao Paulo, Brazil, and is recognized as the market leader in the Brazilian cleaning equipment industry. The purchase agreement with Alfa also provides for additional contingent consideration to be paid if certain future revenue targets are met. Amounts paid under this earn-out will be considered additional purchase price. The earn-out is denominated in foreign currency which approximates $5,200 and is to be calculated based on growth in revenues during the 2009 calendar year, with an interim calculation based on growth in 2008

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revenues. During the first quarter of 2009, we paid the maximum earn-out amount of $1,167 related to the interim period calculation based on growth in 2008 revenues.

On February 29, 2008, we acquired Applied Sweepers, Ltd. (“Applied Sweepers”), a privately-held company based in Falkirk, Scotland, for a purchase price including transaction costs of $68,900 in cash. Applied Sweepers is the manufacturer of Green Machines™ and is recognized as the leading manufacturer of sub-compact outdoor sweeping machines in the United Kingdom. Applied Sweepers also has locations in the United States, France and Germany and sells through a broad distribution network around the world.

The components of the purchase prices of the business combinations described above have been allocated as follows:

Current Assets	$ 14,994
Identified intangible assets	34,443
Goodwill	48,205
Other long-term assets	6,822
Total assets acquired	104,464
Current liabilities	11,278
Long-term liabilities	9,219
Total liabilities assumed	20,497
Net assets acquired	$ 83,967

The following pro forma condensed consolidated financial results of operations for the three months ended March 31, 2009 and 2008 are presented as if the Applied Sweepers and Alfa acquisitions had been completed at the beginning of each period presented. Hewlett was not a business combination and therefore was not included and Shanghai ShenTan and Applied Cleansing have been excluded from the pro forma consolidated condensed financial results of operations for the three months ended March 31, 2009 as these entities were distributors of Tennant or Applied Sweepers products prior to their respective acquisition dates and therefore have no impact to pro forma net sales and an insignificant impact to pro forma net earnings (loss) and pro forma earnings (loss) per share.

	Three Months Ended March 31	
	2009	2008
Pro forma net sales	$ 128,647	$ 177,771
Pro forma net earnings (loss)	(41,746)	5,610
Pro forma earnings (loss) per share:		
Basic	(2.29)	0.30
Diluted	(2.29)	0.30
Weighted average common shares outstanding:		
Basic	18,262,257	18,441,002
Diluted	18,262,257	18,844,504

These pro forma condensed consolidated financial results have been prepared for comparative purposes only and include certain adjustments, such as increased Interest Expense on acquisition debt. The adjustments do not reflect the effect of synergies that would have been expected to result from the integration of these acquisitions. The unaudited pro forma information does not purport to be indicative of the results of operations that actually would have resulted had the combination occurred on January 1 of each period presented or of future results of the consolidated entities.

Divestitures

On June 20, 2008, we completed the sale of certain assets related to our Centurion product to Wayne Sweepers LLC ("Wayne Sweepers") and agreed not to compete with this specific type of product in North America for a period of two years from the date of sale. In exchange for these assets, we received $100 in cash and financed the remaining purchase price of $525 to Wayne Sweepers over a period of three and a half years and began receiving equal quarterly payments of approximately $38 in the fourth quarter of 2008. As a result of this divestiture, we recorded a pre-tax gain of $229 in Profit from Operations in our 2008 Consolidated Statement of Earnings and a reduction primarily to property, plant and equipment. We will also receive

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approximately an additional $900 in royalty payments on the first approximately 250 units manufactured and sold by Wayne Sweepers. These royalty payments will be received and recognized quarterly as the units are sold.

5. Inventories

Inventories are valued at the lower of cost or market. Inventories at March 31, 2009 and December 31, 2008 consisted of the following:

	March 31, 2009	December 31, 2008
Inventories carried at LIFO:		
Finished goods	$ 47,593	$ 52,289
Raw materials, production parts and work-in-process	21,273	17,468
LIFO reserve	(32,405)	(32,481)
Total LIFO inventories	36,461	37,276
Inventories carried at FIFO:		
Finished goods	16,210	17,200
Raw materials, production parts and work-in-process	14,092	12,352
Total FIFO inventories	30,302	29,552
Total inventories	$ 66,763	$ 66,828

The LIFO reserve approximates the difference between LIFO carrying cost and FIFO.

6. Goodwill and Intangible Assets

Goodwill represents the excess of cost over the fair value of net assets of businesses acquired. In accordance with SFAS No. 142, we test Goodwill on an annual basis and when an event occurs or circumstances change that may reduce the fair value of one of our reporting units below its carrying amount. A Goodwill impairment loss occurs if the carrying amount of a reporting unit's Goodwill exceeds its fair value.

During the first quarter of 2009, the price of our stock decreased to the point that our carrying amount exceeded our market capitalization for a period of time leading up to and including March 31, 2009. Accordingly, we performed interim impairment tests as of March 31, 2009 on our Goodwill and other intangible assets. For purposes of performing our interim Goodwill impairment analysis, consistent with our year end 2008 annual impairment analysis, we identified our reporting units as North America; Europe, Middle East, Africa (“EMEA”); Asia Pacific and Latin America. As quoted market prices are not available for our reporting units, estimated fair value was determined using an average weighting of both projected discounted future cash flows and the use of comparative market multiples. The use of comparative market multiples (the market approach) compares the Company to other comparable companies based on valuation multiples to arrive at a fair value. The use of projected discounted future cash flows (discounted cash flow approach) is based on management’s assumptions including forecasted revenues and margins, estimated capital expenditures, depreciation, amortization and discount rates. Changes in economic and operating conditions that occur after the annual impairment analysis or an interim impairment analysis, and that impact these assumptions, may result in a future goodwill impairment charge.

Upon performing the Step 1 test for the interim impairment analysis, the estimated fair values of the North America, Asia Pacific, and Latin America reporting units exceeded their carrying amounts. However, the Company determined that the fair value of the EMEA reporting unit was below its carrying amount, indicating a potential goodwill impairment existed. Having determined that the goodwill of the EMEA reporting unit was potentially impaired, the Company performed Step 2 of the goodwill impairment analysis which involved calculating the implied fair value of its goodwill by allocating the fair value of the reporting unit to all of its assets and liabilities other than goodwill (including both recognized and unrecognized intangible assets) and comparing the residual value to the carrying amount of goodwill. As of March 31, 2009, as a result of our interim impairment tests, we recorded an impairment loss related to our EMEA reporting unit, which totaled $43,363, representing 100% of the Goodwill for this reporting unit. As of March 31, 2009, we did not have an impairment of our other intangible assets.

The income tax benefit associated with the goodwill impairment was $1,074 which relates to the tax deductible portion of the goodwill impairment.

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The changes in the carrying value of goodwill for the three months ended March 31, 2009 are as follows:

	Three Months Ended March 31
Balance at December 31, 2008	$ 62,095
Additions	1,550
Impairment	(43,363)
Foreign currency fluctuations	(1,246)
Balance at March 31, 2009	$ 19,036

The balances of acquired intangible assets, excluding goodwill, are as follows:

	Customer Lists, Service Contracts and Order Book	Trade Name	Technology	Total
Balance as of March 31, 2009:				
Original cost	$ 29,758	$ 6,659	$ 4,284	$ 40,701
Accumulated amortization	(2,983)	(657)	(931)	(4,571)
Foreign currency fluctuations	(6,476)	(1,697)	(581)	(8,754)
Carrying value	$ 20,299	$ 4,305	$ 2,772	$ 27,376
Weighted-average original life (in years)	14	3	12	
Balance as of December 31, 2008:				
Original cost	$ 29,866	$ 6,659	$ 4,285	$ 40,810
Accumulated amortization	(2,463)	(573)	(847)	(3,883)
Foreign currency fluctuations	(6,067)	(1,633)	(486)	(8,186)
Carrying value	$ 21,336	$ 4,453	$ 2,952	$ 28,741
Weighted-average original life (in years)	14	3	12	

The additions to Goodwill and Intangible Assets during the first quarter of 2009 were based on the finalization of the purchase price allocations of Applied Sweepers and Alfa and preliminary purchase price allocations of Shanghai ShenTan and Applied Cleansing as described in Note 4.

Amortization expense on intangible assets for the three months ended March 31, 2009 and 2008 was $688 and $311, respectively.

Estimated aggregate amortization expense based on the current carrying value of amortizable intangible assets for each of the five succeeding years is as follows:

Remaining 2009	$ 2,904

2010		3,872
2011		3,866
2012		2,215
2013		1,829
Thereafter		12,690
Total	$	27,376

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7. Short-Term Borrowings and Long-Term Debt

Debt and weighted average interest rate on debt outstanding are summarized as follows:

	March 31, 2009	December 31, 2008
Short-term borrowings:		
Bank borrowings	$ -	$ -
Long-Term Debt:		
Bank borrowings	58	63
Credit facility borrowings	83,500	87,500
Collateralized borrowings	1,984	1,758
Capital lease obligations	6,345	6,018
Total Long-Term Debt	91,887	95,339
Less: current portion	4,253	3,946
Long-term portion	$ 87,634	$ 91,393

As of March 31, 2009, we had lines of credit totaling approximately $134,277. There were $83,500 in outstanding borrowings under these facilities as of March 31, 2009. In addition, we had stand alone letters of credit of approximately $2,655 outstanding and bank guarantees in the amount of approximately $968. The weighted average interest rate on Long-Term Debt at March 31, 2009 was 3.5%. Commitment fees on unused lines of credit for the quarter ended March 31, 2009 were $70.

Credit Facilities
JPMorgan Chase Bank

On June 19, 2007, we entered into a Credit Agreement (the “Credit Agreement”) with JPMorgan Chase Bank, National Association, as administrative agent, Bank of America, N.A., as syndication agent, BMO Capital Markets Financing, Inc. and U.S. Bank National Association, as Co-Documentation Agents and the Lenders from time to time party thereto. The Credit Agreement provides us and certain of our foreign subsidiaries access to a $125,000 revolving credit facility until June 19, 2012. Borrowings may be denominated in U.S. dollars or certain other currencies. The facility is available for general corporate purposes, working capital needs, share repurchases and acquisitions. The Credit Agreement contains customary representations, warranties and covenants, including but not limited to covenants restricting our ability to incur indebtedness and liens and to merge or consolidate with another entity. Further, the Credit Agreement initially contained a covenant requiring us to maintain indebtedness to EBITDA ratio as of the end of each quarter of not greater than 3.5 to 1 and to maintain an EBITDA to interest expense ratio of no less than 3.5 to 1.

On February 21, 2008, we amended the Credit Agreement to increase the sublimit on foreign currency borrowings from $75,000 to $125,000 and to increase the sublimit on borrowings by the foreign subsidiaries from $50,000 to $100,000.

On March 4, 2009, we entered into a second amendment to the Credit Agreement. This amendment principally provides: (i) an exclusion from our EBITDA calculation for: all non-cash losses and charges, up to $15,000 cash restructuring charges during the 2008 fiscal year and up to $3,000 cash restructuring charges during the 2009 fiscal year, (ii) an amendment of the indebtedness to EBITDA financial ratio required for the second and third quarters of

2009 to not greater than 4.0 to 1 and 5.5 to 1, respectively, (iii) an amendment to the EBITDA to interest expense financial ratio for the third quarter of 2009 to not less than 3.25 to 1, and (iv) the ability for us to incur up to an additional $80,000 of indebtedness pari passu with the lenders under the Credit Agreement. The revolving credit facility available under the Credit Agreement remains at $125,000, but the amendment reduced the expansion feature under the Credit Agreement from $100,000 to $50,000. The amendment put a cap on permitted new acquisitions of $2,000 for the 2009 fiscal year and the amount of permitted new acquisitions in fiscal years after 2009 will be limited according to our then current leverage ratio. The amendment prohibits us from conducting share repurchases during the 2009 fiscal year and limits the payment of dividends and repurchases of stock in fiscal years after 2009 to an amount ranging from $12,000 to $40,000 based on our leverage ratio after giving effect to such payments. Finally, if we obtain additional indebtedness as permitted under the amendment, to the extent that any revolving loans under the credit agreement are then outstanding we are required to prepay the revolving loans in an amount equal to 100% of the proceeds from the additional indebtedness. Additionally, proceeds over $25,000 and under $35,000 will reduce the revolver commitment on a 50% dollar for dollar basis and proceeds over $35,000 will reduce the revolver commitment on a 100% dollar for dollar basis.

In conjunction with the amendment to the Credit Agreement, we gave the lenders a security interest on most of our personal property and pledged 65% of the stock of all domestic and first tier foreign subsidiaries. The obligations under the Credit

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Agreement are also guaranteed by our domestic subsidiaries and those subsidiaries also provide a security interest in their similar personal property.

Included in the amendment were increased interest spreads and increased facility fees. The fee for committed funds under the Credit Agreement now ranges from an annual rate of 0.30% to 0.50%, depending on our leverage ratio. Borrowings under the Credit Agreement bear interest at an annual rate of, at our option, either (i) between LIBOR plus 2.2% to LIBOR plus 3.0%, depending on our leverage ratio; or (ii) the highest of (A) the prime rate, (B) the federal funds rate plus 0.50%, and (C) the adjusted LIBOR rate for a one month period plus 1.0%; plus, in any such case under this clause (ii), an additional spread of 1.2% to 2.0%, depending on our leverage ratio.

We were in compliance with all covenants under the Credit Agreement as of March 31, 2009. There was $83,500 in outstanding borrowings under this facility at March 31, 2009, with a weighted average interest rate of 3.5%.

ABN AMRO Bank

We have a committed revolving credit facility with ABN AMRO Bank N.V. (“ABN AMRO”) of 5,000 Euros, or approximately $6,643, for general working capital purposes. As of March 31, 2009, we had bank guarantees in the amount of 729 Euros, or approximately $968, which reduced the available balance of the facility to 4,272 Euros, or approximately $5,676. Borrowings under the facility incur interest generally at a rate of 1.25% over the ABN AMRO base rate as calculated daily on the cleared account balance. This facility may also be used for short-term loans up to 3,000 Euros, or approximately $3,986. The terms and conditions of these loans would be incorporated in a separate short-term loan agreement at the time of the transaction. There was no balance outstanding on this facility at March 31, 2009.

Bank of America

On August 23, 2007, we entered into a revolving credit facility with Bank of America, National Association, Shanghai Branch. This agreement will expire on August 28, 2009 and is denominated in renminbi (“RMB”) in the amount of 13,400 RMB, or approximately $1,960, and is available for general corporate purposes, including working capital needs of our China location. As part of the March 4, 2009 amendment to the Credit Agreement with JPMorgan Chase Bank, this facility with Bank of America was secured with the same assets as noted above under the JPMorgan Chase section. The interest rate on borrowed funds is equal to the People’s Bank of China’s base rate. This facility also allows for the issuance of standby letters of credit, performance bonds and other similar instruments over the term of the facility for a fee of 0.95% of the amount issued. There was no balance outstanding on this facility at March 31, 2009.

Bank of Scotland

On March 31, 2009, we cancelled our committed credit facility with the Bank of Scotland.

Unibanco

During 2008 we entered into a revolving credit facility with Unibanco Bank (“Unibanco”) in Brazil for 1,000 real, or approximately $431. Borrowings under this credit facility generally bear interest at a rate of 0.32% over Future Contracts on Interbank Deposit Certificates (“CDI”). This facility is collateralized by a letter of credit of $625. There was no balance outstanding on this facility at March 31, 2009.

8. Fair Value of Financial Instruments

On January 1, 2008, we adopted SFAS No. 157 (as impacted by FSP FAS 157-1 and FSP FAS 157-2) for financial assets and liabilities. This standard defines fair value, provides guidance for measuring fair value and requires certain disclosures. This standard does not require any new fair value measurements, but rather applies to all other accounting pronouncements that require or permit fair value measurements. This standard does not apply measurements related to share-based payments, nor does it apply to measurements related to inventory.

SFAS No. 157 discusses valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). The statement utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

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

§ Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

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§ Level 3: Unobservable inputs that reflect the reporting entity's own assumptions.

Our population of financial assets and liabilities subject to fair value measurements at March 31, 2009 are as follows:

	Fair Value	Level 1	Level 2	Level 3
Assets:				
Cash and Cash Equivalents	$ 26,699	$ 26,699	$ -	$ -
Total Assets	$ 26,699	$ 26,699	$ -	$ -
Liabilities:				
Foreign currency forward exchange contracts	596	-	596	-
Total Liabilities	$ 596	$ -	$ 596	$ -

Cash and Cash Equivalents are valued at their carrying amounts in the Condensed Consolidated Balance Sheets, which are reasonable estimates of their fair value due to their short maturities. Our foreign currency forward exchange contracts are valued at fair market value, which is the amount we would receive or pay to terminate the contracts at the reporting date. The fair market value of our Long-Term Debt approximates cost, based on the borrowing rates currently available to us for bank loans with similar terms and remaining maturities.

We use derivative instruments to manage exposures to foreign currency only in an attempt to limit underlying exposures from currency fluctuations and not for trading purposes. As of March 31, 2009 and 2008, the fair value of such contracts outstanding was a net loss of $596 and a net– loss of $68, respectively. At March 31, 2009 and 2008, the notional amounts of foreign currency forward exchange contracts outstanding were $57,463 and $101,438, respectively.

9. Retirement Benefit Plans

As of March 31, 2009, we had four defined benefit pension plans and a postretirement medical plan, which are described in Note 11 of the 2008 Annual Report on Form 10-K. We have contributed $60 and $288 during the first quarter of 2009 to our pension plans and to our postretirement medical plan, respectively.

Recent market conditions have resulted in an unusually high degree of volatility that increased the risks and short-term liquidity associated with certain investments held by the U.S. Pension Plan, which could impact the value of investments after the date of these financial statements. There has been a negative return on Plan assets through March 31, 2009 which could ultimately affect the funded status of the Plan. The ultimate impact on the funded status will be determined based upon market conditions in effect when the annual valuation for the year ended December 31, 2009 is performed. If a cash contribution is deemed necessary, it would be required to be paid no later than September 15, 2010.

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The components of the net periodic benefit cost for the three months ended March 31, 2009 and 2008 were as follows:

	Three Months Ended March 31	
	2009	2008
Pension Benefits:		
Service cost	$ 201	$ 222
Interest cost	593	643
Expected return on plan assets	(734)	(808)
Recognized actuarial (gain) loss	(12)	(57)
Amortization of transition (asset) obligation	(5)	(6)
Amortization of prior service cost	139	139
Foreign currency	(33)	65
Net periodic benefit cost	$ 149	$ 198
Postretirement Medical Benefits:		
Service cost	$ 36	$ 31
Interest cost	207	193
Amortization of prior service cost	(145)	(145)
Net periodic benefit cost	$ 98	$ 79

10. Guarantees

We record a liability for warranty claims at the time of sale. The amount of the liability is based on the trend in the historical ratio of claims to sales, the historical length of time between the sale and resulting warranty claim, new product introductions and other factors. Warranty periods on machines generally range from one to four years. The changes in warranty reserve balances for the three months ended March 31, 2009 and 2008 were as follows:

	Three Months Ended March 31	
	2009	2008
Beginning balance	$ 6,018	$ 6,950
Additions charged to expense	1,436	2,143
Acquired reserves	17	-
Foreign currency fluctuations	(68)	164
Claims paid	(1,868)	(2,154)
Ending balance	$ 5,535	$ 7,103

Certain operating leases for vehicles contain residual value guarantee provisions, which would become due at the expiration of the operating lease agreement if the fair value of the leased vehicles is less than the guaranteed residual value. Of those leases that contain residual value guarantees, the aggregate residual value at lease expiration is $11,277, of which we have guaranteed $8,905. As of March 31, 2009, we have recorded a liability for the estimated end of term loss related to this residual value guarantee of $837 for certain vehicles within our fleet. Our fleet also contains vehicles we estimate will settle at a gain. Gains on these vehicles will be recognized at the end of the lease term.

11. Income Tax

We and our subsidiaries are subject to U.S. federal income tax as well as income tax of numerous state and foreign jurisdictions. We are generally no longer subject to U.S. federal tax examinations for taxable years before 2007 and with limited exceptions, state and foreign income tax examinations for taxable years before 2004.

We recognize potential accrued interest and penalties related to unrecognized tax benefits in Income Tax Expense (Benefit). Included in the net liability of $7,249 for unrecognized tax benefits as of March 31, 2009 was approximately $463 for accrued

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interest and penalties. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be revised and reflected as an adjustment of the Income Tax Expense (Benefit).

We are currently undergoing income tax examinations in various state and foreign jurisdictions covering 2004 to 2007 for which settlement is expected prior to year end. Although the final outcome of these examinations cannot be currently determined, we believe that we have adequate reserves with respect to these examinations.

12. Stock-Based Compensation

The following table presents the components of stock-based compensation expense for the three months ended March 31, 2009 and 2008:

	Three Months Ended March 31	
	2009	2008
Stock options and stock appreciation rights	$ 107	$ 69
Restricted share awards	194	226
Performance share awards	-	240
Share-based liabilities	(15)	20
Total stock-based compensation expense	$ 286	$ 555

During the first three months of 2009 we granted 32,266 restricted shares. The grant date fair value of each share awarded was $10.08. Restricted share awards typically have a two or three year vesting period from the effective date of grant. The total fair value of shares vested during the three months ended March 31, 2009 and 2008 was $133 and $771, respectively.

In 2009, we granted a combination of stock options and restricted share awards to key employees as part of our management compensation program and did not grant performance share awards. These stock options and restricted share awards vest over a three year period and do not contain a performance requirement and are therefore included in the table above in their applicable captions.

We recorded profit sharing expense during 2008 of $2,335 and in order to preserve cash, we chose to entirely fund our profit sharing by issuing shares of Common Stock during the first quarter of 2009. In the first quarter of 2008, our 2007 profit sharing was funded by a combination of stock and cash.

13. Earnings (Loss) Per Share Computations

The computations of basic and diluted earnings (loss) per share are as follows:

	Three Months Ended March 31	
	2009	2008
Numerator:		
Net Earnings (Loss)	$ (41,746)	$ 5,235
Denominator:		
Basic - weighted average outstanding shares	18,262,257	18,441,002
Effect of dilutive securities:		

Employee stock options	-	403,502
Diluted - weighted average outstanding shares	18,262,257	18,844,504
Basic Earnings (Loss) per Share	$ (2.29)	$ 0.28
Diluted Earnings (Loss) per Share	$ (2.29)	$ 0.28

Excluded from the dilutive securities shown above were options to purchase 1,257,904 and 18,437 shares of Common Stock during the three months ended March 31, 2009 and 2008, respectively. These exclusions are made if the exercise prices of these options are greater than the average market price of our Common Stock for the period, if the number of shares we can repurchase exceed the weighted shares outstanding in the options, or if we have a net loss, as the effects are anti-dilutive.

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14. Comprehensive Income (Loss)

We report Accumulated Other Comprehensive Income (Loss) as a separate item in the Shareholders' Equity section of the Condensed Consolidated Balance Sheets. Comprehensive Income (Loss) is comprised of Net Earnings (Loss) and Other Comprehensive Income (Loss). For the three months ended March 31, 2009 and 2008 Other Comprehensive Income (Loss) consisted of foreign currency translation adjustments and amortization of pension items as required by SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" ("SFAS No. 158"). The reconciliations of Net Earnings (Loss) to Comprehensive Income (Loss) are as follows:

	Three Months Ended March 31	
	2009	2008
Net Earnings (Loss)	$ (41,746)	$ 5,235
Foreign currency translation adjustments	(2,599)	2,388
Pension adjustments	(24)	(68)
Comprehensive Income (Loss)	$ (44,369)	$ 7,555

15. Segment Reporting

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," establishes disclosure standards for segments of a company based on management's approach to defining operating segments. In accordance with the objective and basic principles of the standard we aggregate our operating segments, shown below, into one reportable segment that consists of the design, manufacture and sale of products used primarily in the maintenance of nonresidential surfaces. Our products are sold in North America; Europe, Middle East and Africa; and Other International markets including Asia Pacific and Latin America.

The following table sets forth Net Sales by geographic area (net of intercompany sales):

	Three Months Ended March 31	
	2009	2008
North America	$ 73,367	$ 98,243
Europe, Middle East, Africa	41,087	52,721
Other International	14,193	17,636
Total	$ 128,647	$ 168,600

16. Related Party Transactions

During the first quarter of 2008, we acquired Applied Sweepers and Alfa and entered into lease agreements for certain properties owned by or partially owned by the former owners of these entities. These individuals are now current employees of Tennant. Lease payments made under these lease agreements totaled $66 during the first quarter of 2009.

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

Overview

Tennant Company is a world leader in designing, manufacturing and marketing solutions that help create a cleaner, safer world. We provide equipment, parts and consumables and specialty surface coatings to contract cleaners, end-user businesses, healthcare facilities, schools and local, state and federal governments. We sell our products through our direct sales and service organization and a network of authorized distributors worldwide. Geographically, our customers are primarily located in North America, Europe, the Middle East, Africa, Asia-Pacific and Latin America. We strive to be an innovator in our industry through our commitment to understanding our customers’ needs and using our expertise to create innovative products and solutions. The Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) should be read in conjunction with the MD&A included in our Annual Report on Form 10-K for the year ended December 31, 2008.

Net Loss for the first quarter of 2009 was $41.7 million, or a $2.29 loss per diluted share compared to Net Earnings of $5.2 million, or $0.28 per diluted share, in the first quarter of 2008. The Net Loss in the first quarter of 2009 was primarily due to the $43.4 million Goodwill Impairment Charge, or a $2.32 loss per diluted share, as well as a significant decline in Net Sales of 23.7% due to the continued credit crisis and the global economic conditions. Gross margins declined by 30 basis points which was better than expected as a result of benefits from commodity price deflation and cost reductions, including benefits from the fourth quarter 2008 workforce reduction, were not enough to offset the unfavorable impact of lower production volume through our manufacturing facilities. Selling and Administrative Expense was lower in the first quarter of 2009 as compared to same quarter last year as a result of benefits from the fourth quarter 2008 workforce reduction program, reductions in volume-related expenses, and a decrease in discretionary expenses to align expenses with the lower sales volume.

The workforce reduction program was announced during the fourth quarter of 2008 to resize our worldwide employee base by approximately 8%, or about 240 people. A pretax workforce reduction charge totaling $14.6 million, or $0.65 per diluted share, was recognized in the fourth quarter of 2008 as a result of this program. The workforce reduction was accomplished primarily through the elimination of salaried positions across the organization. This measure is estimated to achieve savings of at least $15 million in 2009 and approximately $20 million in 2010. Additionally, early retirements, elimination of contracted positions and attrition accounted for some of the eliminated positions and contributed to these savings. The pretax charge consisted primarily of severance and outplacement services and was included within Selling and Administrative Expense in the 2008 Consolidated Statement of Earnings. In the first quarter of 2009, the severance accrual was revised to reflect actual experience resulting in a benefit of $1.3 million which was included within Selling and Administrative Expense in the 2009 first quarter results of operations.

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Historical Results

The following compares the historical results of operations for the three month periods ended March 31, 2009 and 2008 in dollars and as a percentage of Net Sales (dollars in thousands, except per share data):

	Three Months Ended March 31			
	2009	%	2008	%
Net Sales	$ 128,647	100.0	$ 168,600	100.0
Cost of Sales	75,922	59.0	98,960	58.7
Gross Profit	52,725	41.0	69,640	41.3
Operating Expense:				
Research and Development Expense	5,692	4.4	6,038	3.6
Selling and Administrative Expense	45,460	35.3	55,079	32.7
Goodwill Impairment Charge	43,363	33.7	-	-
Total Operating Expenses	94,515	73.5	61,117	36.2
Profit (Loss) from Operations	(41,790)	(32.5)	8,523	5.1
Other Income (Expense):				
Interest Income	111	0.1	313	0.2
Interest Expense	(652)	(0.5)	(488)	(0.3)
Net Foreign Currency Transaction Gains (Losses)	(361)	(0.3)	(759)	(0.5)
ESOP Income	243	0.2	702	0.4
Other Income (Expense), Net	20	-	5	-
Total Other Income (Expense), Net	(639)	(0.5)	(227)	(0.1)
Profit (Loss) Before Income Taxes	(42,429)	(33.0)	8,296	4.9
Income Tax Expense (Benefit)	(683)	(0.5)	3,061	1.8
Net Earnings (Loss)	$ (41,746)	(32.5)	$ 5,235	3.1
Earnings (Loss) per Diluted Share	$ (2.29)		$ 0.28	

Net Sales

Consolidated Net Sales for the first quarter of 2009 totaled $128.6 million, a 23.7% decline compared to Net Sales of $168.6 million in the first quarter of 2008. The components of the change in consolidated Net Sales in the first quarter of 2009 as compared to the first quarter of 2008 were as follows:

	% Change from 2008
Organic Growth:	
Volume	(22%)
Price	1%
	(21%)
Foreign Currency	(6%)
Acquisitions	3%
Total	(24%)

The 23.7% decrease in consolidated Net Sales in the first quarter of 2009 from 2008 was primarily driven by:

- an organic decline of 21%, driven almost entirely by a decline in our base business volume due to the global economic downturn;

- an unfavorable direct foreign currency exchange impact of 6%; and
- an increase of 3% in sales due to our March 28, 2008 acquisition of Alfa and our February 29, 2008 acquisition of Applied Sweepers.

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The following table sets forth the Net Sales by geographic area for the three month periods ended March 31, 2009 and 2008 and the percentage change from the prior year (dollars in thousands):

	Three Months Ended March 31		
	2009	2008	%
North America	$ 73,367	$ 98,243	(25.3)
Europe, Middle East and Africa	41,087	52,721	(22.1)
Other International	14,193	17,636	(19.5)
Total	$ 128,647	$ 168,600	(23.7)

North America

North America Net Sales were $73.4 million for the first quarter of 2009, a decrease of 25.3% from the first quarter of 2008. We experienced a decline in unit volume across all product lines, but most significantly within our equipment business. We continued to see a longer sales cycle for our products during the first quarter of 2009, with customers delaying or cancelling their purchases due to broader economic factors. During the first quarter of 2009, Net Sales benefited approximately 1% from price increases taken across all product lines. The direct impact of foreign currency within North America unfavorably impacted Net Sales by approximately 1% during the first quarter of 2009.

Europe, Middle East and Africa

In our markets within Europe, the Middle East and Africa (“EMEA”), Net Sales decreased 22.1% to $41.1 million for the first quarter of 2009 as compared to the first quarter of 2008. An organic decline of approximately 14% accounted for the decrease in the first quarter of 2009 when compared to the same period last year due to lower unit volume more than offsetting benefits from pricing actions. Unfavorable direct foreign currency exchange fluctuations decreased Net Sales by approximately 14% in the first quarter of 2009. Acquisitions added approximately 6% to Net Sales within this market in the first quarter of 2009.

Other International

Our Other International markets are comprised of the following key geographic regions: China and other Asia Pacific markets, Japan, Australia and Latin America. Net Sales in these markets for the first quarter of 2009 totaled $14.2 million, a decrease of 19.5% as compared to the first quarter of 2008. An organic decline of approximately 19% in Net Sales was driven by unit volume decreases primarily in our Latin America markets. Unfavorable direct foreign currency translation exchange effects decreased sales in Other International markets by approximately 8% in the 2009 first quarter. Acquisitions added approximately 8% to Net Sales within this market during the first quarter of 2009.

Gross Profit

Gross margin was 41.0% for the first quarter of 2009 compared with 41.3% reported in the first quarter of 2008. Gross margins declined by 30 basis points which was better than expected as a result of benefits from commodity price deflation and cost reductions, including benefits from the fourth quarter 2008 workforce reduction, were not enough to offset the unfavorable impact of lower production volume through our manufacturing facilities. Additionally, gross margin was impacted by unfavorable foreign currency exchange effects.

Operating Expense

Research & Development Expense

Research and Development ("R&D") Expense in the first quarter of 2009 was $5.7 million and $6.0 million in the first quarter of 2008. R&D Expense as a percentage of Net Sales was 4.4% for the first quarter of 2009 compared to 3.6% in the comparable quarter last year. We are committed to spending between 3% to 4% of Net Sales on our R&D efforts annually. R&D Expense was slightly down on a dollar basis due in part to timing of projects and initiatives between years, but was higher than 4% of Net Sales due to the low level of Net Sales in the first quarter of 2009.

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Selling & Administrative Expense

Selling and Administrative ("S&A") Expense in the first quarter of 2009 decreased $9.6 million, or 17.5%, to $45.5 million from $55.1 million in the first quarter of 2008. Favorable direct foreign currency exchange effects decreased S&A Expense by approximately $2.4 million in the first quarter of 2009. S&A Expense in the 2009 first quarter also included a $1.3 million benefit from the revision to the reserve for the severance and related costs associated with the workforce reduction announced in the fourth quarter of 2008.

The remaining $5.9 million, or approximately 10.7%, decrease in S&A Expense during the 2009 first quarter was due to savings from the workforce reduction along with cost controls and reductions in discretionary spending to better align expenses with sales. Partially offsetting these benefits is the inclusion of expenses related to the February 29, 2008 acquisition of Applied Sweepers and the March 28, 2008 acquisition of Alfa.

S&A Expense as a percentage of Net Sales was 35.3% for the first quarter of 2009, up from 32.7% in the comparable 2008 quarter. Although S&A Expense was lower than in the 2008 first quarter on a dollar basis, the rapid decline in sales still resulted in higher S&A Expense as a percentage of Net Sales during the quarter.

Goodwill Impairment Charge

During the first quarter of 2009, we recorded a Goodwill Impairment Charge of $43.4 million related to our EMEA reporting unit. All but $3.8 million of this charge is not tax deductible.

Other Income (Expense), Net

Interest Income

Interest Income was $0.1 million in the first quarter of 2009, a decrease of $0.2 million from 2008. The decrease between 2009 and 2008 reflects the impact of a decline in interest rates between periods on lower average levels of cash and cash equivalents.

Interest Expense

Interest Expense was $0.7 million in the first quarter of 2009, an increase of $0.2 million from 2008 as we became a net debtor during the latter part of the first quarter of 2008 borrowing against our revolving credit facility, primarily to fund the two acquisitions that closed during the first quarter of 2008.

Net Foreign Currency Transaction Gains (Losses)

The net favorable change from the prior year of foreign currency losses for the three month period ended March 31, 2009 of $0.4 million was primarily due to a $0.9 million unfavorable movement in the foreign currency exchange rates in the first quarter of 2008 related to a deal contingent non-speculative forward contract that we entered into which fixed the cash outlay in US dollars for the Alfa acquisition.

ESOP Income

ESOP Income was $0.2 million in the first quarter of 2009 as compared to $0.7 million in the same period in 2008 due to a lower average stock price during the first quarter of 2009. We benefit from ESOP Income when the shares held by Tennant's ESOP Plan are utilized and the basis of those shares is lower than the current average stock price. This benefit is offset in periods when the number of shares needed exceeds the number of shares available from the ESOP as the shortfall must be issued at the current market rate, which is generally higher than the basis of the ESOP shares.

Other Income (Expense), Net

Other Expense, Net was essentially unchanged between the first quarters of 2009 and 2008.

Income Taxes

The effective tax rate in the first quarter of 2009 was negative 1.6% compared to the effective rate in the first quarter of the prior year of 36.9%. The tax expense for the first quarter includes only a $1.1 million tax benefit associated with the $43.4 million impairment of goodwill, materially impacting the overall effective rate.

Excluding the tax benefit associated with the goodwill impairment, the first quarter effective tax rate would have been 41.9%. The increase in the effective rate as compared to the first quarter of the prior year was primarily related to the mix in expected full year taxable earnings by country.

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Liquidity and Capital Resources

Liquidity

Cash and cash equivalents totaled $26.7 million at March 31, 2009, compared to $29.3 million at December 31, 2008. We believe that the combination of internally generated funds and present capital resources are more than sufficient to meet our cash requirements for the next twelve months. Our debt-to-capital ratio was 35.7% and 31.2% at March 31, 2009 and December 31, 2008, respectively.

Cash Flow Summary

Cash provided by (used in) our operating, investing and financing activities is summarized as follows (dollars in thousands):

	Three Months Ended March 31	
	2009	2008
Operating Activities	$ 11,173	$ (5,887)
Investing Activities:		
Purchases of Property, Plant and Equipment, Net of Disposals	(3,561)	(7,408)
Acquistions of Businesses, Net of Cash Acquired	(2,295)	(81,365)
Financing Activities	(7,627)	86,547
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(276)	312
Net Increase (Decrease) in Cash and Cash Equivalents	$ (2,586)	$ (7,801)

Operating Activities

Operating activities provided $11.2 million of cash for the three months ended March 31, 2009. Cash provided by operating activities was driven primarily by reductions in receivables during the quarter, partially offset by lower Employee Compensation and Benefit liabilities due to severance payments associated with the workforce reduction announced in the fourth quarter of 2008.

In the comparable 2008 period, cash used by operating activities was $5.9 million. Cash used by operating activities was driven by a decrease in cash income taxes paid, a decrease in Employee Compensation and Benefits and Other Accrued Expenses and Accounts Payable. The decrease in Employee Compensation and Benefits and Other Accrued Expenses was primarily a result of payments of prior fiscal year performance awards, annual rebates, incentives and profit sharing. Timing of payments was the primary reason for the decrease in Accounts Payable.

Management evaluates how effectively we utilize two of our key operating assets, receivables and inventories, using accounts receivable “Days Sales Outstanding” (DSO) and “Days Inventory on Hand” (DIOH), on a FIFO basis. The metrics are calculated on a rolling three month basis in order to more readily reflect changing trends in the business. These metrics for the quarters ended were as follows (in days):

	March 31, 2009	December 31, 2008	March 31, 2008
DSO	75	77	67
DIOH	121	101	95

At March 31, 2009, DSO increased eight days compared to March 31, 2008 primarily due to decreased sales volume experienced during the first quarter of 2009 and a slowing of payments due to current economic conditions and the decreased availability of credit to our customers. At March 31, 2009, DSO decreased two days compared to December 31, 2008 primarily due to the lower level of sales and the collection of outstanding Accounts Receivable.

At March 31, 2009, DIOH increased twenty-six days compared to March 31, 2008 and increased twenty days compared to December 31, 2008 primarily due to the decline in sales volume experienced during the first quarter of 2009 as well as higher inventory levels due to higher demo and used inventories related to the introduction of new products and higher inventories at our Louisville distribution center and China locations due to longer lead times for products sourced from low-cost regions.

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Investing Activities

Investing activities during the three months ended March 31, 2009 used $5.9 million in cash. Investing activities included net capital expenditures of $3.6 million and $2.3 million related to acquisition of businesses. Investments in capital expenditures included technology upgrades, tooling related to new product development and investments in our Minnesota facilities to complete the new global R&D center of excellence to support new product innovation efforts. The $2.3 million related to acquisitions was primarily comprised of the first quarter earn-out payment for our February 29, 2008 acquisition of Alfa.

Full-year capital spending is anticipated to approximate $15 million or less, including capital spending related to our recent acquisitions.

Investing activities during the three months ended March 31, 2008 used $88.8 million in cash. Investing activities included the acquisitions of Applied Sweepers and Alfa for $81.4 million and capital expenditures of $7.4 million during the three months ended March 31, 2008. Investments in capital expenditures included technology upgrades and new product development.

Financing Activities

Net cash used by financing activities was $7.6 million during the first three months of 2009, primarily from repayment of debt of $4.0 million and $2.4 million in dividends paid.

Net cash provided by financing activities was $86.5 million during the first three months of 2008, primarily from borrowings totaling $92.5 million from our Credit Agreement with our bank group led by JP Morgan. Significant uses of cash included $3.6 million for repurchases of common stock under our share repurchase program and $2.4 million in dividend payments.

Indebtedness

As of March 31, 2009, we had available lines of credit totaling $134.3 million and stand alone letters of credit of approximately $2.7 million. There were $83.5 million in outstanding borrowings under these facilities and we were in compliance with all debt covenants as of March 31, 2009.

On March 4, 2009, we entered into a second amendment to the Credit Agreement with JPMorgan. This amendment principally provides: (i) an exclusion from our EBITDA calculation for: all non-cash losses and charges up to $15.0 million cash restructuring charges during the 2008 fiscal year and up to $3.0 million cash restructuring charges during the 2009 fiscal year, (ii) an amendment of the indebtedness to EBITDA financial ratio required for the second and third quarters of 2009 to not greater than 4.0 to 1 and 5.5 to 1, respectively, (iii) an amendment to the EBITDA to interest expense financial ratio for the third quarter of 2009 to not less than 3.25 to 1, and (iv) the ability for us to incur up to an additional $80.0 million of indebtedness pari passu with the lenders under the Credit Agreement. The revolving credit facility available under the Credit Agreement remains at $125.0 million, but the amendment reduced the expansion feature under the Credit Agreement from $100.0 million to $50.0 million. The amendment put a cap on permitted new acquisitions of $2.0 million for the 2009 fiscal year and the amount of permitted new acquisitions in fiscal years after 2009 will be limited according to our then current leverage ratio. The amendment prohibits us from conducting share repurchases during the 2009 fiscal year and limits the payment of dividends and repurchases of stock in fiscal years after 2009 to an amount ranging from $12.0 million to $40.0 million based on our leverage ratio after giving effect to such payments. Finally, if we obtain additional indebtedness as permitted under the amendment, to the extent that any revolving loans under the credit agreement are then outstanding we are required to prepay the revolving loans in an amount equal to 100% of the proceeds from the additional indebtedness. Additionally, proceeds over $25.0 million and under $35.0 million will reduce the revolver commitment on a 50% dollar for dollar basis and proceeds over $35.0 million will reduce the revolver commitment on a 100% dollar for dollar basis.

In conjunction with the amendment to the Credit Agreement, we gave the lenders a security interest on most of our personal property and pledged 65% of the stock of all domestic and first tier foreign subsidiaries. The obligations under the Credit Agreement are also guaranteed by our domestic subsidiaries and those subsidiaries also provide a security interest in their similar personal property.

Included in the amendment were increased interest spreads and increased facility fees. The fee for committed funds under the Credit Agreement now ranges from an annual rate of 0.30% to 0.50%, depending on our leverage ratio. Borrowings under the Credit Agreement bear interest at an annual rate of, at our option, either (i) between LIBOR plus 2.2% to LIBOR plus 3.0%, depending on our leverage ratio; or (ii) the highest of (A) the prime rate, (B) the federal funds rate plus 0.50%, and (C) the adjusted LIBOR rate for a one month period plus 1.0%; plus, in any such case under this clause (ii), an additional spread of 1.2% to 2.0%, depending on our leverage ratio.

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We were in compliance with all covenants under the Credit Agreement as of March 31, 2009. There was $83.5 million in outstanding borrowings under this facility at March 31, 2009, with a weighted average interest rate of 3.5%.

Contractual Obligations

There have been no material changes with respect to contractual obligations as disclosed in our 2008 Annual Report on Form 10-K.

New Accounting Pronouncements

In December 2008, the FASB issued FSP FAS 132(R)-1, “Employers’ Disclosures about Postretirement Benefit Plan Assets” (“FSP FAS 132(R)-1”). FSP FAS 132(R)-1 provides guidance on an employer’s disclosures about plan assets of a defined benefit pension or other postretirement plan. The requirements are effective for fiscal years beginning after December 15, 2009. This staff position pertains only to the disclosures and does not affect the accounting for defined benefit pensions or other postretirement plans; therefore, we do not anticipate that the adoption of FSP FAS 132(R)-1 will have an impact on our Consolidated Financial Statements.

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” (“SFAS No. 162”). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles. SFAS No. 162 directs the hierarchy to the entity, rather than the independent auditors, as the entity is responsible for selecting accounting principles for financial statements that are presented in conformity with generally accepted accounting principles. The Standard is effective 60 days following SEC’s approval of the Public Company Accounting Oversight Board amendments to remove the hierarchy of generally accepted accounting principles from the auditing standards. We do not expect that SFAS No. 162 will have an impact on our Consolidated Financial Statements.

In April 2009, the FASB issued FSP 157-4, “Interim Disclosures about Fair Value Financial Instruments” (“FSP FAS 157-4”) that provides guidance on how to determine the fair value of assets and liabilities under SFAS No. 157 in the current economic environment and reemphasizes that the objective of fair-value measurement remains an exit price. The requirements are effective for interim and annual periods ending after June 15, 2009. We do not anticipate that the adoption of FSP FAS 157-4 will have an impact on our Consolidated Financial Statements.

In April 2009, the FASB issued FSP FASB 107-1 and APB 28-1, “Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly” (“FSP FASB 107-1 and APB 28-1”) which requires publicly traded companies, as defined in Opinion 28, to disclose the fair value of financial instruments within the scope of Statement 107 in interim financial statements, adding to the current requirement to make those disclosures in annual financial statements. The requirements are effective for interim periods ending after June 15, 2009. We do not anticipate that the adoption of FSP FASB 107-1 and APB 28-1 will have an impact on our Consolidated Financial Statements.

Cautionary Statement Relevant to Forward-Looking Information

Certain statements contained in this document as well as other written and oral statements made by us from time to time are considered “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act. These statements do not relate to strictly historical or current facts and provide current expectations or forecasts of future events. Any such expectations or forecasts of future events are subject to a variety of factors.

These include factors that affect all businesses operating in a global market as well as matters specific to us and the markets we serve.

Particular risks and uncertainties presently facing us include:

- Geopolitical, economic and credit market uncertainty throughout the world.
- Cost and availability of financing for ourselves and our suppliers.
- Our customers’ ability to obtain credit to fund equipment purchases.
- Successful integration of acquisitions, including ability to carry remaining goodwill at current values.
- Ability to accurately project future financial and operating results and to achieve such projections.
- Ability to achieve operational efficiencies while reducing expenses and headcount.
- Fluctuations in the cost or availability of raw materials and purchased components.
- Ability to achieve anticipated global sourcing cost reductions.
- · Success and timing of new technologies and products.

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- Unforeseen product quality problems.
- Effects of litigation, including threatened or pending litigation.
- Relative strength of the U.S. dollar, which affects the cost of our materials and products purchased and sold internationally.
- Ability to effectively manage organizational changes, including workforce reductions.
- Ability to achieve anticipated savings from our workforce reductions.
- Ability to attract and retain key personnel.
- Effects of potential impairment write-down of our intangible asset values.
- Ability to acquire, retain and protect proprietary intellectual property rights.
- Potential for increased competition in our business.
- Changes in laws, including changes in accounting standards and taxation changes.

We caution that forward-looking statements must be considered carefully and that actual results may differ in material ways due to risks and uncertainties both known and unknown. Shareholders, potential investors and other readers are urged to consider these factors in evaluating forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. For additional information about factors that could materially affect Tennant’s results, please see our other Securities and Exchange Commission filings, including the “Risk Factors” section of our 2008 Annual Report on Form 10-K.

We do not undertake to update any forward-looking statement, and investors are advised to consult any further disclosures by us on this matter in our filings with the Securities and Exchange Commission and in other written statements we make from time to time. It is not possible to anticipate or foresee all risk factors, and investors should not consider any list of such factors to be an exhaustive or complete list of all risks or uncertainties.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Commodity Risk – We are subject to exposures resulting from potential cost increases related to our purchase of raw materials or other product components. We do not use derivative commodity instruments to manage our exposures to changes in commodity prices such as steel, oil, gas, lead and other commodities.

Various factors beyond our control affect the price of oil and gas, including but not limited to worldwide and domestic supplies of oil and gas, political instability or armed conflict in oil-producing regions, the price and level of foreign imports, the level of consumer demand, the price and availability of alternative fuels, domestic and foreign governmental regulation, weather-related factors and the overall economic environment. We purchase petroleum-related component parts for use in our manufacturing operations. In addition, our freight costs associated with shipping and receiving product and sales and service vehicle fuel costs are impacted by fluctuations in the cost of oil and gas.

Fluctuations in worldwide demand and other factors affect the price for lead, steel and related products. We do not maintain an inventory of raw or fabricated steel or batteries in excess of near-term production requirements. As a result, fluctuations in the price of lead or steel can significantly impact the cost of our lead and steel-based raw materials and component parts.

During 2008, our raw materials and other purchased component costs were unfavorably impacted by commodity prices although we were able to mitigate these higher costs with pricing actions and cost reduction actions. We will continue to focus on mitigating the risk of continued future raw material or other product component cost increases through product pricing, negotiations with our vendors and cost reduction actions. The success of these efforts will depend upon our ability to increase our selling prices in a competitive market and our ability to achieve cost savings. If the commodity prices increase, our results may be unfavorably impacted in 2009.

Foreign Currency Exchange Risk – Due to the global nature of our operations, we are subject to exposures resulting from foreign currency exchange fluctuations in the normal course of business. Our primary exchange rate exposures are with the Euro, British pound, Australian and Canadian dollars, Japanese yen, Chinese yuan and Brazilian real against the U.S. dollar. The direct financial impact of foreign currency exchange includes the effect of translating profits from local currencies to U.S. dollars, the impact of currency fluctuations on the transfer of goods between Tennant operations in the United States and abroad and transaction gains and losses. In addition to the direct financial impact, foreign currency exchange has an indirect financial impact on our results, including the effect on sales volume within local economies and the impact of pricing actions taken as a result of foreign exchange rate fluctuations.

Because a substantial portion of our products are manufactured or sourced primarily from the United States, a stronger U.S. dollar generally has a negative impact on results from operations outside the United States while a weaker dollar generally has a positive effect. Our objective in managing the exposure to foreign currency fluctuations is to minimize the earnings effects associated with foreign exchange rate changes on certain of our foreign currency-denominated assets and liabilities. We periodically enter into various contracts, principally forward exchange contracts, to protect the value of certain of our foreign currency-denominated assets and liabilities. The gains and losses on these contracts generally approximate changes in the value of the related assets and

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liabilities. We had forward exchange contracts outstanding in the notional amounts of approximately $57.5 million and $101.4 million as of the period ended March 31, 2009 and 2008, respectively. The potential for material loss in fair value of foreign currency contracts outstanding and the related underlying exposures as of March 31, 2009, from a 10% adverse change is unlikely due to the short-term nature of our forward contracts. Our policy prohibits us from entering into transactions for speculative purposes.

Other Matters – Management regularly reviews our business operations with the objective of improving financial performance and maximizing our return on investment. As a result of this ongoing process to improve financial performance, we may incur additional restructuring charges in the future which, if taken, could be material to our financial results.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Principal Financial and Accounting Officer, have evaluated the effectiveness of our disclosure controls and procedures for the period ended March 31, 2009 (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based on that evaluation, our Chief Executive Officer and our Principal Financial and Accounting Officer have concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is communicated to our management, including our principal executive and our principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control

There were no changes in our internal controls over financial reporting during the most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II – OTHER INFORMATION

Item 1. Legal Proceedings

There have been no material changes in our legal proceedings from those disclosed in our 2008 Annual Report on Form 10-K.

Item 1A. Risk Factors

There have been no material changes in our risk factors from those disclosed in our 2008 Annual Report on Form 10-K.

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

On May 3, 2007, the Board of Directors authorized the repurchase of 1,000,000 shares of our common stock. Share repurchases are made from time to time in the open market or through privately negotiated transactions, primarily to offset the dilutive effect of shares issued through our stock-based compensation programs. In order to preserve cash, we had temporarily suspended these repurchases. Our March 4, 2009 amendment to our Credit Agreement prohibits us from conducting share repurchases during the 2009 fiscal year and limits the payment of dividends and repurchases of stock in fiscal years after 2009 to an amount ranging from $12.0 million to $40.0 million based on our leverage ratio after giving effect to such payments.

For the Quarter Ended March 31, 2009	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased
January 1 - 31, 2009	14	$ 15.80	-	288,874
February 1 - 28, 2009	401	12.90	-	288,874
March 1 - 31, 2009	974	8.37	-	288,874
Total	1,389	$ 9.75	-	288,874

(1) Includes 1,389 shares delivered or attested to in satisfaction of the exercise price and/or withholding obligations by employees who exercised stock options or restricted stock under employee compensation plans.

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Item 6. Exhibits

Exhibits

Item #	Description	Method of Filing
3i	Restated Articles of Incorporation	Incorporated by reference to Exhibit 3i to the Company's report on Form 10-Q for the quarterly period ended June 30, 2006.
3ii	Certificate of Designation	Incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2006.
3iii	Amended and Restated By-Laws	Incorporated by reference to Exhibit 3ii to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1999.
10.1	Amendment No. 2 to Credit Agreement dated as of March 4, 2009	Incorporated by reference to Exhibit 10.1 to the Company's Form 8-K dated March 4, 2009.
10.2	Pledge and Security Agreement dated as of March 4, 2009	Incorporated by reference to Exhibit 10.2 to the Company's Form 8-K dated March 4, 2009.
31.1	Rule 13a-14(a)/15d-14(a) Certification of CEO	Filed herewith electronically.
31.2	Rule 13a-14(a)/15d-14(a) Certification of CFO	Filed herewith electronically.
32.1	Section 1350 Certification of CEO	Filed herewith electronically.
32.2	Section 1350 Certification of CFO	Filed herewith electronically.

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.

		TENNANT COMPANY
Date:	May 11, 2009	/s/ H. Chris Killingstad H. Chris Killingstad President and Chief Executive Officer
Date:	May 11, 2009	/s/ Thomas Paulson Thomas Paulson Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)