UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

(mark one)

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended January 3, 2009

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-11406

KADANT INC.

(Exact name of registrant as specified in its charter)

Delaware	**52-1762325**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
One Technology Park Drive **Westford, Massachusetts**	**01886**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code: (978) 776-2000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $.01 par value	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. Yes ☐ No ☒

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

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

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

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

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

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

The aggregate market value of the voting and non-voting common equity held by nonaffiliates of the registrant as of June 28, 2008, was approximately $299,736,000.

As of February 13, 2009, the registrant had 12,549,797 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement pursuant to Regulation 14A promulgated under the Securities Exchange Act of 1934, as amended, to be used in connection with the registrant's 2009 Annual Meeting of Shareholders are incorporated by reference into Part III of this Form 10-K.

Kadant Inc.
Annual Report on Form 10-K
for the Fiscal Year Ended January 3, 2009

Table of Contents

PART I

Forward-Looking Statements

This Annual Report on Form 10-K and the documents that we incorporate by reference in this Report include forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. These forward-looking statements are not statements of historical fact, and may include statements regarding possible or assumed future results of operations. Forward-looking statements are subject to risks and uncertainties and are based on the beliefs and assumptions of our management, using information currently available to our management. When we use words such as “believes,” “expects,” “anticipates,” “intends,” “plans,” “estimates,” “should,” “likely,” “will,” “would,” or similar expressions, we are making forward-looking statements.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties, and assumptions. Our future results of operations may differ materially from those expressed in the forward-looking statements. Many of the important factors that will determine these results and values are beyond our ability to control or predict. You should not put undue reliance on any forward-looking statements. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events, or otherwise. For a discussion of important factors that may cause our actual results to differ materially from those suggested by the forward-looking statements, you should read carefully the section captioned “Risk Factors” in Part I, Item 1A, of this Report.

Item 1. Business

General Development of Business

We were incorporated in Delaware in November 1991 to be the successor-in-interest to several papermaking equipment businesses of Thermo Electron Corporation (Thermo Electron). In November 1992, we completed an initial public offering of a portion of our outstanding common stock. On July 12, 2001, we changed our name to Kadant Inc. from Thermo Fibertek Inc. In August 2001, Thermo Electron disposed of its remaining equity interest in Kadant by means of a stock dividend to its shareholders. Our common stock is listed on the New York Stock Exchange, where it trades under the symbol “KAI.”

The terms “we,” “us,” “our,” “Registrant,” or “Company” in this Report refer to Kadant Inc. and its consolidated subsidiaries.

Description of Our Business

We are a leading supplier of equipment used in the global papermaking and paper recycling industries and also a manufacturer of granules made from papermaking byproducts. Our continuing operations are comprised of one reportable operating segment, Pulp and Papermaking Systems (Papermaking Systems), and two separate product lines reported in Other Businesses, which include Fiber-based Products and, until its sale in April 2007, Casting Products. In classifying operational entities into a particular segment, we considered how our management assesses performance and makes operating decisions, and aggregated businesses with similar economic characteristics, products and services, production processes, customers, and methods of distribution. In addition, prior to its sale in 2005, our subsidiary, Kadant Composites LLC, operated a composite building products business, which is presented as a discontinued operation in the accompanying consolidated financial statements.

Papermaking Systems

Our Papermaking Systems segment has a long and well-established history of developing, manufacturing, and marketing equipment for the global papermaking and paper recycling industries. Some of our businesses or their predecessor companies have been in operation for more than 100 years. Our customer base includes major global paper manufacturers and, with our equipment found in most of the world's pulp and paper mills, we believe we have one of the largest installed bases of equipment in the pulp and paper industry. We manufacture our products in ten countries in Europe, North and South America, and Asia.

In 2005, we acquired all the outstanding stock of The Johnson Corporation (Kadant Johnson), a leading supplier of fluid-handling systems and equipment, including steam and condensate systems, components, and controls. These products are used primarily in the dryer section of the papermaking process and during the production of corrugated boxboard, metals, plastics, rubber, textiles, and food. In 2006*, our subsidiary, Kadant Light Machinery (Jining) Co., Ltd. (Kadant Jining), acquired substantially all of the assets of Jining Huayi Light Industry Machinery Co., Ltd. (Huayi), a supplier of stock-preparation equipment in China.

Our Papermaking Systems segment consists of the following product lines: stock-preparation systems and equipment, fluid-handling systems and equipment, paper machine accessory equipment, and water-management systems.

Stock-preparation systems and equipment

We develop, manufacture, and market complete custom-engineered systems and equipment, as well as standard individual components, for pulping, de-inking, screening, cleaning, and refining recycled and virgin fibers to prepare them for entry into the paper machine during the production of recycled paper. Our principal stock-preparation products include:

– Recycling and approach flow systems: Our equipment includes pulping, screening, cleaning, and de-inking systems that blend pulp mixtures and remove contaminants, such as ink, glue, metals, and other impurities, to prepare them for entry into the paper machine during the production of recycled paper.
– Virgin pulping process equipment: Our equipment includes pulp washing, evaporator, recausticizing, and condensate treatment systems used to remove lignin, concentrate and recycle process chemicals, and remove condensate gases.

Fluid-handling systems and equipment

We develop, manufacture and market rotary joints, precision unions, steam and condensate systems, components, and controls used primarily in the dryer section of the papermaking process and during the production of corrugated boxboard, metals, plastics, rubber, textiles, and food. Our principal fluid-handling systems include:

– Rotary joints: Our mechanical devices, used with rotating shafts, allow the transfer of pressurized fluid from a stationary source into and out of rotating machinery for heating, cooling, or the transfer of fluid power.
– Syphons: Our devices, installed primarily inside the rotating cylinders of paper machines, are used to force steam once it has cooled into a liquid state (condensate) out of the drying cylinders through rotary joints located on either end.
– Turbulator® tube bars: Our steel or stainless steel axial bars, installed on the inside of dryers, are used to induce turbulence in the condensate layer to improve the uniformity and rate of heat transfer (drying rate) of the dryers.
– Engineered steam and condensate systems: Our systems control the flow of steam from the boiler to the paper drying cylinders, collect condensed steam, and return it to the boiler to improve energy-efficiency during the paper drying process.

* Unless otherwise noted, references to 2008, 2007, and 2006 in this Annual Report on Form 10-K are for the fiscal years ended January 3, 2009, December 29, 2007, and December 30, 2006, respectively.

Paper machine accessory equipment

We develop, manufacture, and market a wide range of doctor systems and related consumables that continuously clean papermaking rolls to keep paper machines running efficiently; doctor blades made of a variety of materials to perform functions including cleaning, creping, web removal, and application of coatings; and profiling systems that control moisture, web curl, and gloss during paper production. Our principal paper machine accessory products include:

– Doctor systems and holders: Our doctor systems clean papermaking rolls to maintain the efficient operation of paper machines by placing a blade against the roll at a constant and uniform pressure. A doctor system consists of the structure supporting the blade and the blade holder. A large paper machine may have as many as 100 doctor systems.
– Profiling systems: We offer profiling systems that control moisture, web curl, and gloss during paper production.
– Doctor blades: We manufacture doctor blades made of a variety of materials including metal, bi-metal, or synthetic materials that perform a variety of functions including cleaning, creping, web removal, or the application of coatings. A typical doctor blade has a life ranging from eight hours to two months, depending on the application.

Water-management systems

We develop, manufacture, and market water-management systems and equipment used to continuously clean paper machine fabrics, drain water from pulp mixtures, form the sheet or web, and filter the process water for reuse. Our principal water-management systems include:

– Shower and fabric-conditioning systems: Our shower and fabric-conditioning systems assist in the removal of contaminants that collect on paper machine fabrics used to convey the paper web through the forming, pressing, and drying sections of the paper machine. The average paper machine has between 3 and 12 fabrics. These fabrics can easily become contaminated with fiber, fillers, pitch, and dirt that can have a detrimental effect on paper machine performance and paper quality. Our shower and fabric-conditioning systems assist in the removal of these contaminants.
– Formation systems: We supply structures that drain, purify, and recycle process water from the pulp mixture during paper sheet and web formation.
– Water-filtration systems: We offer a variety of filtration systems and strainers that remove contaminants from process water before reuse and recover reusable fiber for recycling back into the pulp mixture.

Other Businesses

Our other businesses include our Fiber-based Products business and, until its sale on April 30, 2007, our Casting Products business, which manufactured grey and ductile iron castings.

Our Fiber-based Products business produces biodegradable, absorbent granules from papermaking byproducts for use primarily as carriers for agricultural, home lawn and garden, and professional lawn, turf and ornamental applications, as well as for oil and grease absorption.

Discontinued Operation

In 2005, our Kadant Composites LLC subsidiary (Composites LLC) sold substantially all of its assets to LDI Composites Co. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including warranty obligations related to products manufactured prior to the sale date. Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business.

Through the sale date, Composites LLC offered a standard limited warranty to the owners of its decking and roofing products, limited to repair or replacement of the defective product or a refund of the original purchase price. Composites LLC records the minimum amount of the potential range of loss for products under warranty in accordance with Statement of Financial Accounting Standards (SFAS) No. 5, "Accounting for Contingencies" (SFAS 5). As of January 3, 2009, the accrued warranty costs associated with the composites business were $2.1 million, which represent the low end of the estimated range of warranty reserve required based on the level of claims received by Composites LLC through the end of 2008. Composites LLC has calculated that the total potential warranty cost ranges from $2.1 million to approximately $13.1 million. The high end of the range represents the estimated maximum level of warranty claims remaining based on the total sales of the products under warranty. Composites LLC will continue to record adjustments to accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments known to be entered against it in litigation, if any.

All activity related to this business is classified in the results of the discontinued operation in the accompanying consolidated financial statements.

Composites LLC's inability to pay or process warranty claims has exposed us to greater risks associated with litigation. For more information regarding our current litigation arising from these claims, see Part I, Item 3, "Legal Proceedings," and Part I, Item 1A, "Risk Factors".

Research and Development

We develop a broad range of products for all facets of the markets we serve. We focus our research and development efforts on the technological advancement of our stock-preparation, fluid-handling, paper machine accessory, and water-management products.

Our research and development expenses from continuing operations were $6.2 million, $6.0 million, and $6.2 million in 2008, 2007, and 2006, respectively.

Raw Materials

Raw materials, components, and supplies for our significant products are available either from a number of different suppliers or from alternative sources that we believe could be developed without a material adverse effect on our business.

The raw material used in the manufacture of our fiber-based granules is obtained from three paper recycling mills. Although we believe that our relationships with the mills are good, the mills may not continue to supply sufficient raw material. In the past, we have experienced some difficulty in obtaining sufficient raw material to operate at optimal production levels. We continue to work with the mills to ensure a stable supply of raw material. To date, we have been able to meet all of our customer delivery requirements, but there can be no assurance that we will be able to meet future delivery requirements. If the mills were unable or unwilling to supply us sufficient fiber, we would be forced to find an alternative supplier for this raw material.

Patents, Licenses, and Trademarks

We protect our intellectual property rights by applying for and obtaining patents when appropriate. We also rely on technical know-how, trade secrets, and trademarks to maintain our competitive position. We also enter into license agreements with others to grant and/or receive rights to patents and know-how.

Papermaking Systems

We have numerous U.S. and foreign patents, including foreign counterparts to our U.S. patents, expiring on various dates ranging from 2009 to 2029. No particular patent, or related group of patents, is so important that its loss would significantly affect our operations. From time to time, we enter into licenses of products with other companies that serve the pulp, papermaking, converting, and paper recycling industries.

Other Businesses

We currently hold several U.S. patents, expiring on various dates ranging from 2009 to 2021, related to various aspects of the processing of fiber-based granules and the use of these materials in the agricultural, professional turf, home lawn and garden, general absorption, oil and grease absorption, and catbox filler markets. We also have foreign counterparts to certain of these U.S. patents in Canada.

Seasonal Influences

Papermaking Systems

There are no material seasonal influences on this segment's sales of products and services.

Other Businesses

Our fiber-based granular products business experiences fluctuations in sales, usually in the third and fourth quarters, when sales decline due to the seasonality of the agricultural and home lawn and garden markets.

Working Capital Requirements

There are no special inventory requirements or credit terms extended to customers that would have a material adverse effect on our working capital.

Dependency on a Single Customer

No single customer accounted for more than 10% of our consolidated revenues or more than 10% of the Papermaking Systems segment's revenues in any of the past three years. During 2008, 2007, and 2006, approximately 61% of our sales were to customers outside the United States, principally in China and Europe. Revenues from China were $44.2 million, $76.6 million, and $71.3 million in 2008, 2007, and 2006, respectively, representing 13%, 21%, and 21% of total revenues, respectively.

Backlog

Our backlog of firm orders for the Papermaking Systems segment was $64.6 million and $108.6 million at year-end 2008 and 2007, respectively. We anticipate that substantially all of the backlog at January 3, 2009 will be shipped or completed during the next 12 months. Some of these orders can be canceled by the customer upon payment of a cancellation fee.

Competition

We face significant competition in each of our principal markets. We compete primarily on the basis of quality, price, service, technical expertise, and product performance and innovation. We believe the reputation that we have established for quality products and in-depth process knowledge provides us with a competitive advantage. In addition, a significant portion of our business is generated from our existing worldwide customer base. To maintain this base, we have emphasized technology, service, and a problem-solving relationship with our customers.

We are a leading supplier of stock-preparation equipment used for the preparation of recycled and virgin fibers in the production of recycled paper. Several major competitors supply various pieces of equipment for this process. Our principal competitors in this market are Voith Paper GmbH, Groupe Laperriere & Verrault Inc., Metso Corporation, and Maschinenfabrik Andritz AG. We compete in this market primarily on the basis of technical expertise, product innovation, and price. Other competitors specialize in segments within the white- and brown-paper markets.

We are a leading supplier of fluid-handling systems and equipment, offering global sales and service, application expertise, and an extensive rotary joint product line. There are numerous competitors in this market, including Deublin Company, Barco Company, Christian Maier GmbH & Co. KG, and Duff-Norton Company. In addition, we compete with numerous local competitors. We generally compete in this market based on process knowledge, technical competency, product and service quality, and price.

We are a leading supplier of specialty accessory equipment for paper machines. Our principal global competitors in this market are Joh. Clouth GmbH & Co. KG and Metso Corporation. Because of the high capital cost of paper machines and the role of our accessories in maintaining the efficiency of these machines, we generally compete in this market on the basis of service, technical expertise, performance, and price.

In our water-management product line, various competitors exist in the formation, shower and fabric-conditioning systems, and filtration systems markets. Principal competitors are IBS-Paper Performance Group in formation and shower and fabric-conditioning systems and Asten/Johnson Foils in formation tables. In addition, a variety of smaller companies compete within the shower and fabric-conditioning systems and filtration systems markets. In each of these markets, we generally compete on the basis of process knowledge, application experience, product quality, service, and price.

Environmental Protection Regulations

We believe that our compliance with federal, state, and local environmental protection regulations will not have a material adverse effect on our capital expenditures, earnings, or competitive position.

Employees

As of January 3, 2009, we had approximately 1,800 employees worldwide.

Financial Information

Financial information concerning our segment and product lines is summarized in Part IV, Item 15, Exhibits and Financial Statement Schedules, Note 11 to the audited consolidated financial statements, which begins on page F-1 of this Report.

Financial information about exports by domestic operations and about foreign operations is summarized in Part IV, Item 15, Exhibits and Financial Statement Schedules, Note 11 to the audited consolidated financial statements, which begins on page F-1 of this Report.

Available Information

We file annual, quarterly, and current reports, proxy statements, and other documents with the Securities and Exchange Commission (SEC) under the Exchange Act. The public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Also, the SEC maintains a website that contains reports, proxy and information statements, and other information regarding issuers, including us, that file electronically with the SEC. The public can obtain any documents that we file with the SEC at www.sec.gov. We also make available free of charge through our website at www.kadant.com our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to these Reports filed with or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after we electronically file these materials with, or furnish them to, the SEC. We are not including the information contained in our website as part of this Report nor are we incorporating the information on our website into this Report by reference.

Executive Officers of the Registrant

The following table summarizes certain information concerning individuals who are our executive officers as of March 1, 2009:

Name	Age	Present Title (Fiscal Year First Became Executive Officer)
William A. Rainville	67	Chairman of the Board, President, and Chief Executive Officer (1991)
Edward J. Sindoni	64	Executive Vice President and Chief Operating Officer (1994)
Thomas M. O'Brien	57	Executive Vice President and Chief Financial Officer (1994)
Jonathan W. Painter	50	Executive Vice President (1997)
Eric T. Langevin	46	Senior Vice President (2006)
Sandra L. Lambert	53	Vice President, General Counsel, and Secretary (2001)
Michael J. McKenney	47	Vice President, Finance and Chief Accounting Officer (2002)

Mr. Rainville has been president and chief executive officer since our incorporation in 1991, a member of our board of directors since 1992, and chairman of our board since 2001. Prior to our spin-off in 2001, Mr. Rainville also held various managerial positions with Thermo Electron, including chief operating officer, recycling and resource recovery, a position he held since 1998, and for more than five years prior to that, senior vice president. Prior to joining Thermo Electron, Mr. Rainville held positions at Drott Manufacturing, Paper Industry Engineering, and Sterling Pulp and Paper.

Mr. Sindoni was named an executive vice president and our chief operating officer in March 2006 and is responsible for global operations. Prior to that, he served as a senior vice president from 2001 to 2006 with responsibility for our paper machine accessory equipment and water-management systems product lines. From 1992 to 2001, he served as a vice president. Prior to joining us in 1987, he had a 21-year career with the General Electric Company.

Mr. O'Brien has been an executive vice president since 1998 and our chief financial officer since 2001. He served as our treasurer from 2001 to February 2005 and also as vice president, finance, from 1991 to 1998. Prior to joining us, Mr. O'Brien held various finance positions at Racal Interlan, Inc., Prime Computer, Compugraphic Corporation, and the General Electric Company.

Mr. Painter has been an executive vice president since 1997 and is responsible for our fiberline business, consisting of our stock-preparation product line and our fiber-based products business. He served as president of our composite building products business from 2001 until its sale in 2005. He also served as our treasurer and treasurer of Thermo Electron from 1994 until 1997. Prior to 1994, Mr. Painter held various managerial positions with us and Thermo Electron.

Mr. Langevin has been a senior vice president since March 2007 and is responsible for our paperline business, consisting of our paper machine accessory equipment, fluid-handling, and water-management systems product lines. He served as vice president, with responsibility for our paper machine accessory equipment and water-management systems product lines, from 2006 to 2007. From 2001 to 2006, Mr. Langevin was president of our Kadant Web Systems Inc. subsidiary and before that served as its senior vice president and vice president of operations. Prior to 2001, Mr. Langevin managed several product groups and departments within Kadant Web Systems after joining us in 1986 as a product development engineer.

Ms. Lambert has been a vice president and our general counsel since 2001, and our secretary since our incorporation in 1991. Prior to joining us, she was a vice president and secretary of Thermo Electron since 1999 and 1990, respectively, and before that was a member of Thermo Electron's legal department.

Mr. McKenney has been our vice president, finance and chief accounting officer since January 2002 and served as our corporate controller from 1997 to 2007. Mr. McKenney was controller of Kadant AES, our division acquired from Albany International Inc., from 1993 to 1997. Prior to 1993, Mr. McKenney held various financial positions at Albany International.

Item 1A. Risk Factors

In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we wish to caution readers that the following important factors, among others, in some cases have affected, and in the future could affect, our actual results and could cause our actual results in 2009 and beyond to differ materially from those expressed in any forward-looking statements made by us, or on our behalf.

Our business is dependent on worldwide and local economic conditions as well as the condition of the pulp and paper industry.

We sell products primarily to the pulp and paper industry, which is a cyclical industry. Generally, the financial condition of the global pulp and paper industry corresponds to the condition of the worldwide economy, as well as to a number of other factors, including pulp and paper production capacity relative to demand. Recently, worldwide equity and credit markets have been experiencing extreme volatility and disruption and the markets in which we sell our products, both globally and locally, are experiencing severe economic downturns, the length of which are difficult to predict. This global uncertainty and turmoil and the recession in many economies have adversely affected demand for our customers’ products, as well as for our products, especially our capital equipment products. Our stock-preparation equipment product line has been particularly affected since it contains a higher proportion of capital products than our other product lines. The slowing of demand as consumer and economic activity declines results in reduced demand for paper and board products. This reduced demand has resulted in an overcapacity situation in many grades of paper, particularly linerboard, in most regions of the world, which adversely affects our capital business. In addition, paper producers are lowering their production rates, which adversely impacts the sales of our products, including parts and consumables. Also, the crisis affecting financial institutions has caused, and is likely to continue to cause, liquidity and credit issues for many businesses, including our customers in the pulp and paper industry as well as other industries, and results in their inability to fund projects, capacity expansion plans and, to some extent, routine operations. We expect these factors to particularly affect planned or proposed projects in developing economies in Eastern Europe and Russia, which have been a source of significant capital expansion projects recently for both our stock-preparation and fluid-handling systems and equipment product lines. These conditions have resulted in a number of structural changes in the pulp and paper industry, including decreased spending, mill closures, consolidations, and bankruptcies, all of which adversely affect our business, revenue, and profitability.

Furthermore, the inability of our customers to obtain credit may affect our ability to recognize revenue and income, particularly on large capital equipment orders from new customers for which we may require letters of credit. We may also be unable to issue letters of credit to our customers, required in some cases to guarantee performance, if the economic crisis continues and we exhaust our existing sources of credit. In addition, paper producers have been and continue to be negatively affected by higher operating costs, especially higher energy and chemical costs.

Paper companies have curtailed their capital and operating spending in the current economic environment and will likely be cautious about resuming spending, if and when market conditions improve. As paper companies consolidate in response to market weakness, they frequently reduce capacity and postpone or even cancel capacity addition or expansion projects. For example, in China, the worsening economic conditions have resulted in an oversupply of linerboard as demand has fallen with the reduction in exports to the U.S. and other countries. Major paper producers in that country have curtailed production to address the oversupply and announced delays or cancellations of several new paper machines used to produce linerboard. Several large projects in our stock-preparation equipment product line in Asia were cancelled or delayed into 2009 or later. These cancellations and delays have adversely affected our 2008 financial results, caused us to lower our expectations of revenues and earnings per share for the 2009 fiscal year, and may negatively impact us in future years as well. Our financial performance for 2009 and potentially longer will also be negatively impacted if there are additional delays in customers securing financing or our customers become unable to secure such financing.

A significant portion of our international sales has, and may in the future, come from China and we operate several manufacturing facilities in China, which exposes us to political, economic, operational and other risks.

We have significant revenues from China, operate significant facilities in China, and expect to manufacture and source more of our equipment and components from China in the future. During 2008 and 2007, approximately $44.2 million, or 13%, and $76.6 million, or 21%, respectively, of our total revenues were from customers in China. Our manufacturing facilities in China, as well as the significant level of revenues from China, expose us to increased risk in the event of economic slowdowns, changes in the policies of the Chinese government, political unrest, unstable economic conditions, or other developments in China or in U.S.-China relations that are adverse to trade, including enactment of protectionist legislation or trade or currency restrictions. In addition, orders from customers in China, particularly for large stock-preparation systems that have been tailored to a customer's specific requirements, have credit risks higher than we generally incur elsewhere, and some orders are subject to the receipt of financing approvals from the Chinese government. For this reason, we do not record signed contracts from customers in China for large stock-preparation systems as orders until we receive the down payments for such contracts. The timing of the receipt of these orders and the down payments are uncertain and there is no assurance that we will be able to recognize revenue on these contracts. We may experience a loss if the contract is cancelled prior to the receipt of a down payment in the event we commence engineering or other work associated with the contract. In addition, we may experience a loss if the contract is cancelled, or the customers do not fulfill their obligations under the contract, prior to the receipt of a letter of credit covering the remaining balance of the contract. Typically, the letter of credit represents 80% or more of the total order.

Worsening economic conditions have led some customers in China to defer, slow down, or cancel planned capital projects, especially those dependent on exports to Western economies, such as linerboard production. These actions will cause us to recognize revenue on certain contracts in periods later than originally anticipated, or not at all.

Certain of our contracts, particularly for stock-preparation and systems orders, require us to provide a standby letter of credit to a customer as beneficiary to guarantee our warranty and performance obligations under the contract. One of our customers in China has indicated its intention to draw upon all of the outstanding standby letters of credit issued to secure our warranty and performance obligations under multiple contracts with that customer for reasons that we believe are unrelated to our warranty and performance obligations. We have and intend to continue to vigorously oppose these draws and any other potential claims, but if we are unsuccessful we could incur a significant expense that would adversely affect our financial results. Furthermore, our future revenues would be negatively affected if this customer were to choose a different supplier.

Our business is subject to economic, currency, political, and other risks associated with international sales and operations.

During 2008 and 2007, approximately 61% of our sales were to customers outside the United States, principally in China and Europe. In addition, we operate several manufacturing operations worldwide, including those in China, Europe, Mexico, and Brazil. International revenues and operations are subject to a number of risks, including the following:

- agreements may be difficult to enforce and receivables difficult to collect through a foreign country's legal system,
- foreign customers may have longer payment cycles,
- foreign countries may impose additional withholding taxes or otherwise tax our foreign income, impose tariffs, adopt other restrictions on foreign trade, impose currency restrictions or enact other protectionist or anti-trade measures,
- worsening economic conditions may result in worker unrest, labor actions, and potential work stoppages,

– it may be difficult to repatriate funds, due to unfavorable tax consequences or other restrictions or limitations imposed by foreign governments, and
– the protection of intellectual property in foreign countries may be more difficult to enforce.

Although we seek to charge our customers in the same currency in which our operating costs are incurred, fluctuations in currency exchange rates may affect product demand and adversely affect the profitability in U.S. dollars of products we provide in international markets where payment for our products and services is made in their local currencies. In addition, our inability to repatriate funds could adversely affect our ability to service our debt obligations. Any of these factors could have a material adverse impact on our business and results of operations. Furthermore, while some risks can be hedged using derivatives or other financial instruments, or may be insurable, such attempts to mitigate these risks may be costly and not always successful.

We are subject to intense competition in all our markets.

We believe that the principal competitive factors affecting the markets for our products include quality, price, service, technical expertise, and product performance and innovation. Our competitors include a number of large multinational corporations that may have substantially greater financial, marketing, and other resources than we do. As a result, they may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sale of their services and products. Competitors' technologies may prove to be superior to ours. Our current products, those under development, and our ability to develop new technologies may not be sufficient to enable us to compete effectively. Competition, especially in China, has increased as new companies enter the market and existing competitors expand their product lines and manufacturing operations.

Adverse changes to the soundness of our suppliers and customers could affect our business and results of operations.

All of our businesses are exposed to risk associated with the creditworthiness of our key suppliers and customers, including pulp and paper manufacturers and other industrial customers, many of which may be adversely affected by the volatile conditions in the financial markets, worldwide economic downturns, and worsening economic conditions. These conditions could result in financial instability, bankruptcy, or other adverse effects at any of our suppliers or customers. The consequences of such adverse effects could include the interruption of production at the facilities of our suppliers, the reduction, delay or cancellation of customer orders, delays in or the inability of customers to obtain financing to purchase our products, and bankruptcy of customers or other creditors. For example, one of our customers in North America, Smurfit-Stone Container Corporation, recently filed for bankruptcy protection, which will adversely affect our revenues and ability to collect on certain receivables, among other things. Any adverse changes to the soundness of our suppliers or customers may adversely affect our cash flow, profitability and financial condition.

Our debt may adversely affect our cash flow and may restrict our investment opportunities.

In 2008, we entered into a five-year unsecured revolving credit facility (2008 Credit Agreement) in the aggregate principal amount of up to $75 million, which includes an uncommitted unsecured incremental borrowing facility of up to an additional $75 million. We had $38 million outstanding under the 2008 Credit Agreement at year-end 2008 and we have also borrowed additional amounts under other agreements to fund our stock repurchase program and grow our business. We may also obtain additional long-term debt and working capital lines of credit to meet future financing needs, which would have the effect of increasing our total leverage.

Our indebtedness could have negative consequences, including:

- increasing our vulnerability to adverse economic and industry conditions,
- limiting our ability to obtain additional financing,
- limiting our ability to pay dividends on or to repurchase our capital stock,
- limiting our ability to acquire new products and technologies through acquisitions or licensing agreements, and
- limiting our flexibility in planning for, or reacting to, changes in our business and the industries in which we compete.

Our existing indebtedness bears interest at floating rates and as a result, our interest payment obligations on our indebtedness will increase if interest rates increase. To reduce the exposure to floating rates, we hedged $23.8 million, or 43%, of our outstanding floating rate debt as of January 3, 2009 through interest rate swap agreements. The unrealized loss associated with these swap agreements was $2.1 million as of January 3, 2009. This unrealized loss represents the estimated amount that the swap agreements could be settled for. If these swap agreements were terminated prior to the scheduled maturity date and if we were required to pay cash for the value of the swap, we would incur a loss, which would adversely affect our financial results.

Our ability to satisfy our obligations and to reduce our total debt depends on our future operating performance and on economic, financial, competitive, and other factors beyond our control. Our business may not generate sufficient cash flows to meet these obligations or to successfully execute our business strategy. If we are unable to service our debt and fund our business, we may be forced to reduce or delay capital expenditures or research and development expenditures, seek additional financing or equity capital, restructure or refinance our debt, or sell assets. We may not be able to obtain additional financing or refinance existing debt or sell assets on terms acceptable to us or at all.

Restrictions in our 2008 Credit Agreement may limit our activities.

Our 2008 Credit Agreement contains, and future debt instruments to which we may become subject may contain, restrictive covenants that limit our ability to engage in activities that could otherwise benefit us, including restrictions on our ability and the ability of our subsidiaries to:

- incur additional indebtedness,
- pay dividends on, redeem, or repurchase our capital stock,
- make investments,
- create liens,
- sell assets,
- enter into transactions with affiliates, and
- consolidate, merge, or transfer all or substantially all of our assets and the assets of our subsidiaries.

We are also required to meet specified financial ratios under the terms of our 2008 Credit Agreement. Our ability to comply with these financial restrictions and covenants is dependent on our future performance, which is subject to prevailing economic conditions and other factors, including factors that are beyond our control such as currency exchange rates, interest rates, changes in technology, and changes in the level of competition.

Our failure to comply with any of these restrictions or covenants may result in an event of default under our 2008 Credit Agreement and other loan obligations, which could permit acceleration of the debt under those instruments and require us to repay the debt before its scheduled due date.

If an event of default were to occur, we may not have sufficient funds available to make the payments required under our indebtedness. If we are unable to repay amounts owed under our debt agreements, those lenders may be entitled to foreclose on and sell the collateral that secures our borrowings under the agreements.

Adverse changes to the soundness of financial institutions could affect us.

We have relationships with many financial institutions, including lenders under our credit facilities and insurance underwriters, and from time to time, we execute transactions with counterparties in the financial industry, such as our interest swap arrangements and other hedging transactions. As a consequence of the recent and continuing volatility in the financial markets, these financial institutions or counterparties could be adversely affected and we may not be able to access credit facilities, complete transactions as intended, or otherwise obtain the benefit of the arrangements we have entered into with such financial parties, which could adversely affect our business and results of operations.

The inability of Kadant Composites LLC to pay claims against it has exposed us to litigation, which if we are unable to successfully defend, could have a material adverse effect on our consolidated financial results.

On October 21, 2005, our Kadant Composites LLC subsidiary (Composites LLC) sold substantially all of its assets to LDI Composites Co. (Buyer) for approximately $11.9 million in cash and the assumption of $0.7 million of liabilities, resulting in a cumulative loss on sale of $0.1 million. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including warranty obligations related to products manufactured prior to the sale date (Retained Liabilities), and, jointly and severally with its parent company Kadant Inc., agreed to indemnify the Buyer against losses caused to the Buyer arising from claims associated with the Retained Liabilities. The indemnification obligation is contractually limited to approximately $8.9 million. All activity related to this business is classified in the results of the discontinued operation in our consolidated financial statements.

Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. We are now co-defendants in a purported consumer class action, together with Composites LLC and another defendant, arising from these warranty claims, in which the plaintiffs claim that such damages exceed $50 million. See Part I, Item 3, “Legal Proceedings” for further information. We could incur substantial costs to defend ourselves and the Buyer under our indemnification obligations in this lawsuit and a judgment or a settlement of the claims against the defendants could have a material adverse impact on our consolidated financial results. Creditors or other claimants against Composites LLC may seek other parties, including us, against whom to assert claims. While we believe any such asserted or possible claims against us or the Buyer would be without merit, the cost of litigation and the outcome, if we were unable to successfully defend such claims, could adversely affect our consolidated financial results.

An increase in the accrual for warranty costs of the discontinued operation adversely affects our consolidated financial results.

The discontinued operation has experienced significant liabilities associated with warranty claims related to its composite decking products manufactured prior to the sale date. The accrued warranty costs of the discontinued operation as of January 3, 2009 represents the low end of the estimated range of warranty costs required to be recorded under SFAS 5 based on the level of claims received through year-end 2008. Composites LLC has calculated that the total potential warranty cost ranges from $2.1 million to approximately $13.1 million. The high end of the range represents the estimated maximum level of warranty claims remaining based on the total sales of the products under warranty. On September 30, 2007, the discontinued operation ceased doing business and has no employees or other service providers to collect or process warranty claims. Composites LLC will continue to record adjustments to accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments entered against it in litigation, which will adversely affect our consolidated results.

Our inability to successfully identify and complete acquisitions or successfully integrate any new or previous acquisitions could have a material adverse effect on our business.

Our strategy includes the acquisition of technologies and businesses that complement or augment our existing products and services. Our most recent acquisition was the Kadant Jining acquisition in June 2006. Any such acquisition involves numerous risks that may adversely affect our future financial performance and cash flows. These risks include:

- competition with other prospective buyers resulting in our inability to complete an acquisition or in us paying substantial premiums over the fair value of the net assets of the acquired business,
- inability to obtain regulatory approval, including antitrust approvals,
- difficulty in assimilating operations, technologies, products and the key employees of the acquired business,
- inability to maintain existing customers or to sell the products and services of the acquired business to our existing customers,
- diversion of management's attention away from other business concerns,
- inability to improve the revenues and profitability or realize the cost savings and synergies expected in the acquisition,
- assumption of significant liabilities, some of which may be unknown at the time,
- potential future impairment of the value of goodwill and intangible assets acquired, and
- identification of internal control deficiencies of the acquired business.

In the fourth quarter of 2008, we recorded a $40.3 million impairment charge to write down the goodwill associated with the stock-preparation reporting unit within our Papermaking Systems segment. We may incur additional impairment charges to write down the value of our goodwill and acquired intangible assets in the future if the assets are not deemed recoverable, which could have a material adverse affect on our operating results.

We may be required to reorganize our operations in response to changing conditions in the worldwide economy and the pulp and paper industry, and such actions may require significant expenditures and may not be successful.

We have undertaken various restructuring measures in response to changing market conditions in the countries in which we operate and in the pulp and paper industry in general, which have affected our business. We may engage in additional cost reduction programs in the future. We may not recoup the costs of programs we have already initiated, or other programs in which we may decide to engage in the future, the costs of which may be significant. In connection with any future plant closures, delays or failures in the transition of production from existing facilities to our other facilities in other geographic regions could also adversely affect our results of operations. In addition, our profitability may decline if our restructuring efforts do not sufficiently reduce our future costs and position us to maintain or increase our sales.

Our fiber-based products business is subject to a number of factors that may adversely influence its profitability, including high costs of natural gas and dependence on a few suppliers of raw materials.

We use natural gas, the price of which is subject to fluctuation, in the production of our fiber-based granular products. We seek to manage our exposure to natural gas price fluctuations by entering into short-term forward contracts to purchase specified quantities of natural gas from a supplier. We may not be able to effectively manage our exposure to natural gas price fluctuations. Higher costs of natural gas will adversely affect our consolidated results if we are unable to effectively manage our exposure or pass these costs on to customers in the form of surcharges.

We are dependent on three paper mills for the fiber used in the manufacture of our fiber-based granular products. Due to process changes at the mills, we have experienced some difficulty obtaining sufficient raw material to operate at optimal production levels. We continue to work with the mills to ensure a stable supply of raw material. To date, we have been able to meet all of our customer delivery requirements, but there can be no assurance that we will be able to meet future delivery requirements. Although we believe our relationships with the mills are good, the mills could decide not to continue to supply sufficient papermaking byproducts, or may not agree to continue to supply such products on commercially reasonable terms. If the mills were unable or unwilling to supply us sufficient fiber, we would be forced to find an alternative supply for this raw material. We may be unable to find an alternative supply on commercially reasonable terms or could incur excessive transportation costs if an alternative supplier were found, which would increase our manufacturing costs, and might prevent prices for our products from being competitive or require closure of the business.

Our inability to protect our intellectual property could have a material adverse effect on our business. In addition, third parties may claim that we infringe their intellectual property, and we could suffer significant litigation or licensing expense as a result.

We seek patent and trade secret protection for significant new technologies, products, and processes because of the length of time and expense associated with bringing new products through the development process and into the marketplace. We own numerous U.S. and foreign patents, and we intend to file additional applications, as appropriate, for patents covering our products. Patents may not be issued for any pending or future patent applications owned by or licensed to us, and the claims allowed under any issued patents may not be sufficiently broad to protect our technology. Any issued patents owned by or licensed to us may be challenged, invalidated, or circumvented, and the rights under these patents may not provide us with competitive advantages. In addition, competitors may design around our technology or develop competing technologies. Intellectual property rights may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture increased market share. We could incur substantial costs to defend ourselves in suits brought against us, including for alleged infringement of third party rights, or in suits in which we may assert our intellectual property rights against others. An unfavorable outcome of any such litigation could have a material adverse effect on our business and results of operations. In addition, as our patents expire, we rely on trade secrets and proprietary know-how to protect our products. We cannot be sure the steps we have taken or will take in the future will be adequate to deter misappropriation of our proprietary information and intellectual property. Of particular concern are developing countries, such as China, where the laws, courts, and administrative agencies may not protect our intellectual property rights as fully as in the United States or Europe.

We seek to protect trade secrets and proprietary know-how, in part, through confidentiality agreements with our collaborators, employees, and consultants. These agreements may be breached, we may not have adequate remedies for any breach, and our trade secrets may otherwise become known or be independently developed by our competitors or our competitors may otherwise gain access to our intellectual property.

Our share price will fluctuate.

Stock markets in general and our common stock in particular have experienced significant price and volume volatility over the past year. The market price and trading volume of our common stock may continue to be subject to significant fluctuations due not only to general stock market conditions but also to a change in sentiment in the market regarding our operations, business prospects, or future funding. Given the nature of the markets in which we participate and the impact of accounting standards related to revenue recognition, we may not be able to reliably predict future revenues and profitability, and unexpected changes may cause us to adjust our operations. A large proportion of our costs are fixed, due in part to our significant selling, research and development, and manufacturing costs. Thus, small declines in revenues could disproportionately affect our operating results. Other factors that could affect our share price and quarterly operating results include:

– failure of our products to pass contractually agreed upon acceptance tests, which would delay or prohibit recognition of revenues under applicable accounting guidelines,

- changes in the assumptions used for revenue recognized under the percentage-of-completion method of accounting,
- failure of a customer, particularly in Asia, to comply with an order's contractual obligations or inability of a customer to provide financial assurances of performance,
- adverse changes in demand for and market acceptance of our products,
- competitive pressures resulting in lower sales prices for our products,
- adverse changes in the pulp and paper industry,
- delays or problems in our introduction of new products,
- delays or problems in the manufacture of our products,
- our competitors' announcements of new products, services, or technological innovations,
- contractual liabilities incurred by us related to guarantees of our product performance,
- increased costs of raw materials or supplies, including the cost of energy,
- changes in the timing of product orders,
- fluctuations in our effective tax rate,
- the operating and share price performance of companies that investors consider to be comparable to us, and
- changes in global financial markets and global economies and general market conditions.

Anti-takeover provisions in our charter documents, under Delaware law, and in our shareholder rights plan could prevent or delay transactions that our shareholders may favor.

Provisions of our charter and bylaws may discourage, delay, or prevent a merger or acquisition that our shareholders may consider favorable, including transactions in which shareholders might otherwise receive a premium for their shares. For example, these provisions:

- authorize the issuance of "blank check" preferred stock without any need for action by shareholders,
- provide for a classified board of directors with staggered three-year terms,
- require supermajority shareholder voting to effect various amendments to our charter and bylaws,
- eliminate the ability of our shareholders to call special meetings of shareholders,
- prohibit shareholder action by written consent, and
- establish advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted on by shareholders at shareholder meetings.

In addition, our board of directors has adopted a shareholder rights plan intended to protect shareholders in the event of an unfair or coercive offer to acquire our company and to provide our board of directors with adequate time to evaluate unsolicited offers. Preferred stock purchase rights have been distributed to our common shareholders pursuant to the rights plan. This rights plan may have anti-takeover effects. The rights plan will cause substantial dilution to a person or group that attempts to acquire us on terms that our board of directors does not believe are in our best interests and those of our shareholders and may discourage, delay, or prevent a merger or acquisition that shareholders may consider favorable, including transactions in which shareholders might otherwise receive a premium for their shares.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

We believe that our facilities are in good condition and are suitable and adequate for our present operations. We do not anticipate significant difficulty in obtaining lease renewals or alternative space as needed. The location and general character of our principal properties as of January 3, 2009 are as follows:

Papermaking Systems

We own approximately 1,841,000 square feet and lease approximately 136,000 square feet, under leases expiring on various dates ranging from 2009 to 2017, of manufacturing, engineering, and office space. In addition, in China we lease the land associated with our buildings under long-term leases, which expire on dates ranging from 2044 to 2054. Our principal engineering and manufacturing facilities are located in Vitry-le-Francois, France; Jining, China; Three Rivers, Michigan, U.S.A; Auburn, Massachusetts, U.S.A; Yanzhou, China; Theodore, Alabama, U.S.A; Queensbury, New York, U.S.A; Weesp, The Netherlands; Wuxi, China; Hindas, Sweden; Guadalajara, Mexico; Bury, England; Summerstown, Ontario, Canada; Sao Paulo, Brazil; Mason, Ohio, U.S.A; and Duren, Germany.

Corporate and Other Businesses

We lease approximately 12,000 square feet in Westford, Massachusetts, for our corporate headquarters under a lease expiring in 2013. We own approximately 31,000 square feet of manufacturing and office space located in Green Bay, Wisconsin. We also lease approximately 25,000 square feet of manufacturing space located in Green Bay, Wisconsin, on a tenant-at-will basis.

Item 3. Legal Proceedings

We have been named as a co-defendant, together with Composites LLC and another defendant, in a consumer class action lawsuit filed in the United States District Court for the District of Massachusetts (the Court) on December 27, 2007 on behalf of a putative class of individuals who own GeoDeck™ decking or railing products manufactured by Composites LLC between April 2002 and October 2003. The complaint in this matter purports to assert, among other things, causes of action for unfair and deceptive trade practices, fraud, negligence, breach of warranty and unjust enrichment, and it seeks compensatory damages and punitive damages under various state consumer protection statutes, which plaintiffs claim exceed $50 million. On March 14, 2008, we, Composites LLC, and the other co-defendant filed motions to dismiss all counts in the complaint. On November 19, 2008, the Court dismissed the complaint in its entirety, including all claims against us, Composites LLC, and the other co-defendant. On December 4, 2008, the plaintiffs sought to vacate this order of dismissal in order to amend their complaint, and this motion was denied without prejudice by the Court on January 12, 2009. On January 27, 2009, the plaintiffs renewed their motion to vacate the order of dismissal in order to file an amended complaint, which motion was denied by the Court on March 3, 2009. The plaintiffs have not indicated whether they will attempt to appeal the Court’s order. We intend to defend against this action vigorously, but there is no assurance we will prevail in such defense. We could incur significant costs to defend this lawsuit and a judgment or a settlement of the claims against the defendants could have a material adverse impact on our consolidated financial results.

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

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities

Market Price of Common Stock

Our common stock trades on the New York Stock Exchange under the symbol KAI. The closing market price on the New York Stock Exchange for our common stock on February 13, 2009, was $10.33 per share.

The following table sets forth the high and low sales prices of our common stock for 2008 and 2007, as reported in the consolidated transaction reporting system.

	2008		2007	
Quarter	**High**	**Low**	**High**	**Low**
First	$31.02	$23.17	$27.79	$22.11
Second	30.53	22.29	31.70	24.47
Third	26.08	17.87	31.58	25.06
Fourth	23.86	11.53	33.76	26.85

Holders of Common Stock

As of February 13, 2009, we had approximately 4,822 holders of record of our common stock. This does not include holdings in street or nominee name.

Dividend Policy

We have never declared or paid cash dividends and we do not at this time expect to pay cash dividends in the foreseeable future because our policy has been to use earnings to finance expansion and growth, as well as repurchase our stock. Payment of dividends will rest within the discretion of the board of directors and will depend upon, among other factors, our earnings, capital requirements, and financial condition. Our ability to pay dividends is restricted by the terms of our 2008 Credit Agreement.

Issuer Purchases of Equity Securities

The following table provides information about purchases by us of our common stock during the fourth quarter of 2008:

Issuer Purchases of Equity Securities

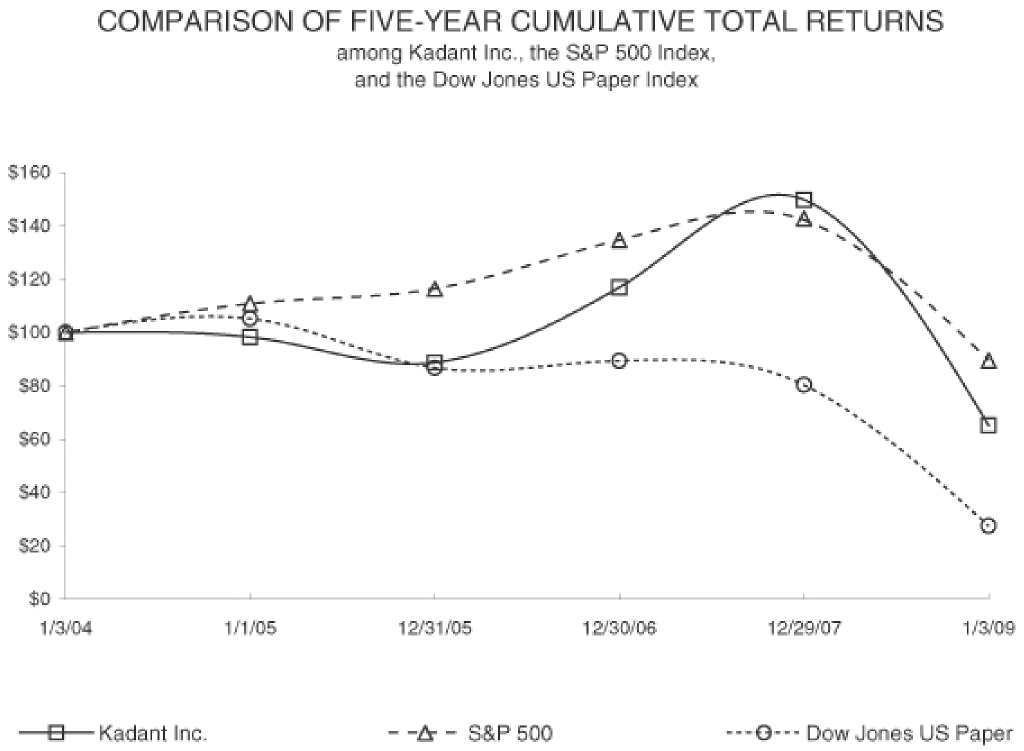
Period	Total Number of Shares Purchased (1)(2)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans (1)(2)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans
9/28/08 – 10/31/08	130,000	15.24	130,000	$ 32,441,860
11/1/08 – 11/30/08	295,500	15.59	295,500	$ 27,834,618
12/1/08 – 01/03/09	63,000	13.19	63,000	$ 27,003,554
Total	488,500	15.19	488,500	

(1) On May 5, 2008, our board of directors approved the repurchase by us of up to $30 million of our equity securities during the period from May 5, 2008 through May 5, 2009. As of January 3, 2009, we had repurchased 1,353,107 shares of our common stock for $30.0 million under this authorization.

(2) On October 22, 2008, our board of directors approved the repurchase by us of up to $30 million of our equity securities during the period from October 22, 2008 through October 22, 2009. Repurchases may be made in public or private transactions, including under Securities Exchange Act Rule 10b-5-1 trading plans. As of January 3, 2009, we had repurchased 204,693 shares of our common stock for $3.0 million under this authorization.

Performance Graph

This performance graph compares the cumulative, five-year total shareholder return assuming an investment of $100 (and the reinvestment of dividends) in our common stock, the Standard & Poor's 500 Stock Index, and the Dow Jones US Paper Index. Our common stock trades on the New York Stock Exchange under the ticker symbol "KAI." Because our fiscal year ends on a Saturday, the graph uses the last trading day of our fiscal year.



	1/3/04	1/1/05	12/31/05	12/30/06	12/29/07	1/3/09
Kadant Inc.	100.00	98.32	88.73	116.93	149.74	65.13
S&P 500	100.00	110.88	116.33	134.70	142.10	89.53
Dow Jones US Paper	100.00	105.21	86.77	89.44	80.16	27.54

The information included under the heading "Performance Graph" in Item 5 of this Annual Report on Form 10-K is "furnished" and not "filed" and shall not be deemed to be "soliciting material" or subject to Regulation 14A , shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933, as amended, or the Exchange Act.

Item 6. Selected Financial Data

(In thousands, except per share amounts)	2008 (a)	2007	2006	2005	2004 (b)
Statement of Operations Data					
Revenues	$329,158	$366,496	$341,613	$243,713	$194,966
(Loss) Income from Continuing Operations	(22,595)	25,418	18,281	9,865	5,753
Income (Loss) from Discontinued Operation, Net of Tax	37	(2,750)	(1,184)	(2,988)	(5,099)
Net (Loss) Income	$ (22,558)	$ 22,668	$ 17,097	$ 6,877	$ 654
Basic (Loss) Earnings per Share:					
Continuing Operations	$ (1.67)	$ 1.80	$ 1.32	$ .71	$ .41
Discontinued Operation	–	(.19)	(.08)	(.21)	(.36)
Net (Loss) Income	$ (1.67)	$ 1.61	$ 1.24	$ .50	$ .05
Diluted (Loss) Earnings per Share:					
Continuing Operations	$ (1.67)	$ 1.78	$ 1.30	$ .70	$ .40
Discontinued Operation	–	(.19)	(.09)	(.21)	(.35)
Net (Loss) Income	$ (1.67)	$ 1.59	$ 1.21	$ .49	$ .05
Balance Sheet Data (c)					
Working Capital (d)	$ 98,017	$107,487	$ 80,542	$ 75,446	$113,650
Total Assets	356,917	437,069	393,085	355,811	285,237
Long-Term Obligations	52,122	30,460	44,652	46,500	–
Shareholders' Investment	192,715	278,751	237,965	207,625	212,461

(a) Reflects a $40.3 million pre-tax goodwill impairment charge, a $15.4 million tax provision related to applying a valuation allowance to certain deferred tax assets, and $3.7 million of pre-tax restructuring costs.

(b) Reflects $9.5 million of pre-tax restructuring costs.

(c) Includes the composite building products business, which is reflected as a discontinued operation.

(d) Includes ($1.9) million, ($1.1) million, $3.0 million, $7.4 million, and $8.1 million in 2008, 2007, 2006, 2005, and 2004, respectively, associated with the discontinued operation.

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

Reference is made throughout this Management’s Discussion and Analysis of Financial Condition and Results of Operations to Notes included in our Consolidated Financial Statements beginning on page F-1 of this Report.

Overview

Company Overview

We are a leading supplier of equipment used in the global papermaking and paper recycling industries and are also a manufacturer of granules made from papermaking byproducts. Our continuing operations are comprised of one reportable operating segment: Pulp and Papermaking Systems (Papermaking Systems), and two product lines reported in Other Businesses, which include Fiber-based Products and, prior to its sale in April 2007, Casting Products. Through our Papermaking Systems segment, we develop, manufacture, and market a range of equipment and products for the global papermaking and paper recycling industries. We have a large, stable customer base that includes most of the world’s major paper manufacturers. We believe our large installed base provides us with a spare parts and consumables business that yields higher margins than our capital equipment business, and which should be less susceptible to the cyclical trends in the paper industry.

Through our Fiber-based Products line, we manufacture and sell granules derived from pulp fiber for use as carriers for agricultural, home lawn and garden, and professional lawn, turf and ornamental applications, as well as for oil and grease absorption. Our Casting Products business manufactured grey and ductile iron castings until its sale on April 30, 2007.

In addition, prior to its sale in 2005, our subsidiary, Composites LLC, operated a composite building products business, which is presented as a discontinued operation in the accompanying consolidated financial statements.

International Sales

During 2008 and 2007, approximately 61% of our sales were to customers outside the United States, principally in China and Europe. We generally seek to charge our customers in the same currency in which our operating costs are incurred. However, our financial performance and competitive position can be affected by currency exchange rate fluctuations affecting the relationship between the U.S. dollar and foreign currencies. We seek to reduce our exposure to currency fluctuations through the use of forward currency-exchange contracts. We may enter into forward contracts to hedge certain firm purchase and sale commitments denominated in currencies other than our subsidiaries’ functional currencies. These contracts hedge transactions principally denominated in U.S. dollars.

Application of Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of our consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Our actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that entail significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies upon which our financial position depends, and which involve the most complex or subjective decisions or assessments, are those described below. For a discussion on the application of these and other accounting policies, see Note 1 in the Notes to Consolidated Financial Statements.

Revenue Recognition and Accounts Receivable. We enter into arrangements with customers that have multiple deliverables, such as equipment and installation, and we recognize revenues and profits on certain long-term contracts using the percentage-of-completion method of accounting.

- *Percentage-of-Completion.* Revenues recorded under the percentage-of-completion method of accounting pursuant to Statement of Position No. 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts," were $58.1 million in 2008, $103.5 million in 2007, and $91.9 million in 2006. The percentage of completion is determined by comparing the actual costs incurred to date to an estimate of total costs to be incurred on each contract. If a loss is indicated on any contract in process, a provision is made currently for the entire loss. Our contracts generally provide for billing of customers upon the attainment of certain milestones specified in each contract. Revenues earned on contracts in process in excess of billings are classified as unbilled contract costs and fees, and amounts billed in excess of revenues are classified as billings in excess of contract costs and fees. The estimation process under the percentage-of-completion method affects the amounts reported in our consolidated financial statements. A number of internal and external factors affect our percentage-of-completion and cost of sales estimates, including labor rate and efficiency variances, estimates of warranty costs, estimated future material prices from vendors, and customer specification and testing requirements. In addition, we are exposed to the risk, primarily relating to our orders in China that a customer will not comply with the order's contractual obligations to take delivery of the equipment. The contractual obligations relating to the order may be difficult to enforce through a foreign country's legal system, which could result in a significant credit exposure in the period or periods that were to be affected by the breach of contract. Although we make every effort to ensure the accuracy of our estimates in the application of this accounting policy, if our actual results differed from our estimates, or if we were to use different assumptions, it is possible that materially different amounts could be reported as revenues in our consolidated financial statements.
- *SAB No. 104.* Under SAB No. 104, "Revenue Recognition," when the terms of sale include customer acceptance provisions, and compliance with those provisions cannot be demonstrated until customer acceptance, revenues are recognized upon such acceptance. When a sale arrangement involves multiple elements (e.g., installation), we consider the guidance in Emerging Issues Task Force (EITF) No. 00-21 "Revenue Arrangements with Multiple Deliverables." Such transactions are evaluated to determine whether the deliverables in the arrangement represent separate units of accounting. If equipment and installation do not meet the separation criteria under EITF No. 00-21, revenues for products sold that require installation, for which the installation is essential to functionality or is not deemed inconsequential or perfunctory, are recognized upon completion of installation. Revenues for products sold where installation is not essential to functionality, and is deemed inconsequential or perfunctory, are recognized upon shipment, with estimated installation costs accrued. We provide a reserve for the estimated warranty and installation costs at the time revenue is recognized, as applicable. To the extent that installation becomes a significant component of our business in the future, the judgment associated with the determination of revenue recognition will increase. The complexity of all issues related to the assumptions, risks, and uncertainties inherent in the application of SAB No. 104 affects the amounts reported as revenues in our consolidated financial statements. Under SAB No. 104, we may not be able to reliably predict future revenues and profitability due to the difficulty of estimating when installation will be performed or when we will meet the contractually agreed upon performance tests, which can delay or prohibit recognition of revenues. The determination of when we install the equipment or fulfill the performance guarantees is largely dependent on our customers, their willingness to allow installation of the equipment or performance of the appropriate tests in a timely manner, and their cooperation in addressing possible problems that would impede achievement of the performance guarantee criteria. Unexpected changes in the timing related to the completion of installation or performance guarantees could cause our revenues and earnings to be significantly affected.

We exercise judgment in determining our allowance for bad debts, which is based on our historical collection experience, current trends, credit policies, specific customer collection issues, and accounts receivable aging categories. In determining this allowance, we look at historical writeoffs of our receivables. We also look at current trends in the credit quality of our customer base as well as changes in our credit policies. We perform ongoing credit evaluations of our customers and adjust credit limits based upon payment history and each customer’s current creditworthiness. We continuously monitor collections and payments from our customers. In addition, in some instances we utilize letters of credit as a way to mitigate credit exposure. While actual bad debts have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same rate of bad debts that we have had in the past, especially in light of current business conditions in the paper industry. A significant change in the liquidity or financial position of any of our customers could result in the uncollectibility of the related accounts receivable and could adversely affect our operating results and cash flows in that period.

Warranty Obligations for Continuing Operations. We offer warranties of various durations to our customers depending upon the specific product and terms of the customer purchase agreement. We typically negotiate terms regarding warranty coverage and length of warranty depending on the products and their applications. Our standard mechanical warranties require us to repair or replace a defective product during the warranty period at no cost to the customer. We record an estimate for warranty-related costs at the time of sale based on our actual historical occurrence rates and repair costs, as well as other analytical tools for estimating future warranty claims. These estimates are revised for variances between actual and expected claims rates. While our warranty costs have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same warranty return rates or repair costs that we have in the past.

A significant increase in warranty occurrence rates or costs to repair our products would lead to an increase in the warranty provision and could have a material adverse impact on our consolidated results for the period or periods in which such returns or additional costs occur.

Warranty Obligations for Discontinued Operation. In 2005, our Kadant Composites LLC subsidiary (Composites LLC) sold substantially all of its assets to LDI Composites Co. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including warranty obligations related to products manufactured prior to the sale date. All activity related to this business is classified in the results of the discontinued operation in the accompanying consolidated financial statements.

Through the second quarter of 2006, Composites LLC recorded an estimate for warranty-related costs at the time of sale based on its actual historical return rates and repair costs, as well as other analytical tools for estimating future warranty claims. These estimates were revised for variances between actual and expected claims rates. Composites LLC’s analysis of expected warranty claims rates included detailed assumptions associated with potential product returns, including the type of product sold, temperatures at the location of installation, density of boards, and other factors. Certain assumptions, such as the effect of weather conditions and high temperatures on the product installed, included inherent uncertainties that contributed to variances between actual and expected claims rates.

During the third quarter of 2006, Composites LLC concluded that the assumptions noted above were not accurately predicting the actual level of warranty claims, making it no longer possible to calculate a reasonable estimate of the future level of potential warranty claims. Accordingly, as no amount within the total range of loss represents a best estimate of the ultimate loss to be recorded, Composites LLC is required under SFAS 5 to record the minimum amount of the potential range of loss for products under warranty. As of January 3, 2009, the accrued warranty costs associated with the composites business were $2.1 million, which represent the low end of the range of potential loss for products under warranty based on the level of claims received through the end of 2008. Composites LLC has calculated that the potential warranty cost ranges from $2.1 million to approximately $13.1 million. The high end of the range represents the estimated maximum level of warranty claims remaining based on the total sales of the products under warranty.

Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. Composites LLC will continue to record adjustments to accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments entered against it in litigation, if any.

Stock-Based Compensation. We issue a variety of stock-based compensation, including stock options and restricted stock unit awards, primarily to our key employees and directors. Compensation expense associated with restricted stock units is recognized ratably over the vesting period based on the grant date fair value.

Determining the amount of stock-based compensation to be recorded for stock options requires us to develop estimates to be used in calculating the grant-date fair value. We did not grant any stock options in 2008, 2007 or 2006. For options granted prior to 2006, we calculated the grant-date fair values using the Black-Scholes valuation model. The use of valuation models requires us to make estimates of the following assumptions:

Expected volatility—We derived the estimated stock price volatility based on a review of our actual historic stock prices commensurate with the expected life of the award.

Expected option life—Our estimate of an expected option life was derived based on a review of our historic option holding periods, including a consideration of the holding period inherent in currently vested, but unexercised options. We believe that this historical data is currently the best estimate of the expected term of a new option.

Risk-free interest rate—We used the yield on zero-coupon U.S. Treasury securities for a period that is commensurate with the expected term assumption as the risk-free interest rate.

The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Pension and Other Retiree Benefits. Several of our U.S. and non-U.S. subsidiaries sponsor defined benefit pension and other retiree benefit plans. The cost and obligations of these arrangements are calculated using many assumptions to estimate the benefits that the employee earns while working, the amount of which cannot be completely determined until the benefit payments cease. Major assumptions used in the accounting for these employee benefit plans include the discount rate, expected return on plan assets and rate of increase in employee compensation levels. Assumptions are determined based on Company data and appropriate market indicators in consultation with third-party actuaries, and are evaluated each year as of the plans' measurement date. Our unfunded benefit obligation related to these plans totaled $11.7 million at year-end 2008. Should any of these assumptions change, they would have an effect on net periodic pension costs and the unfunded benefit obligation.

Income Taxes. We estimate the degree to which tax assets and loss carryforwards will result in a benefit based on expected profitability by tax jurisdiction, and provide a valuation allowance for tax assets and loss carryforwards that we believe will more likely than not go unused. If it becomes more likely than not the tax asset or loss carryforward will be used, we would reverse the related valuation allowance. Our tax valuation allowance totaled $19.1 million at year-end 2008. Should our actual future taxable income by tax jurisdiction vary from our estimate, additional allowances or reversals thereof may be necessary.

We provide a liability for future income tax payments in the worldwide tax jurisdictions in which we operate. Should tax return positions that we expect are sustainable not be sustained upon audit, we could be required to record an incremental tax provision for such taxes. Should previously unrecognized tax benefits be sustained, a reduction in our tax provision would result.

It is our policy to provide for uncertain tax positions and the related interest and penalties based upon management's assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities. At January 3, 2009, we believe that we have appropriately accounted for any unrecognized tax benefits. To the extent we prevail in matters for which a liability for an unrecognized tax benefit is established or are required to pay amounts in excess of the liability, our effective tax rate in a given financial statement period may be affected.

Inventories. We value our inventory at the lower of the actual cost (on a first-in, first-out; or weighted average basis) or market value and include materials, labor, and manufacturing overhead. We regularly review inventory quantities on hand and compare these amounts to historical and forecasted usage of and demand for each particular product or product line. We record a charge to cost of revenues for excess and obsolete inventory to reduce the carrying value of the inventories to net realizable value. Inventory writedowns have historically been within our expectations and the provisions established. A significant decrease in demand for our products could result in an increase in the amount of excess inventory quantities on hand, resulting in a charge for the writedown of that inventory in that period. In addition, our estimates of future product usage or demand may prove to be inaccurate, resulting in an understated or overstated provision for excess and obsolete inventory. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product usage and demand, any significant unanticipated changes in demand or technological developments could have a significant impact on the value of our inventory and our reported operating results.

Derivatives. We use derivative instruments primarily to reduce our exposure to changes in currency exchange rates and interest rates. When we enter into a derivative contract, we make a determination as to whether the transaction is deemed to be a hedge for accounting purposes. For contracts deemed to be a hedge, we formally document the relationship between the derivative instrument and the risk being hedged. In this documentation, we specifically identify the asset, liability, forecasted transaction, cash flow, or net investment that has been designated as the hedged item, and evaluate whether the derivative instrument is expected to reduce the risks associated with the hedged item. To the extent these criteria are not met, we do not use hedge accounting for the derivative.

SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities,” as amended, requires that all derivatives be recognized on the balance sheet at fair value. For derivatives designated as cash flow hedges, the related gains or losses on these contracts are deferred as a component of accumulated other comprehensive items. These deferred gains and losses are recognized in the period in which the underlying anticipated transaction occurs. For derivatives designated as fair value hedges, the unrealized gains and losses resulting from the impact of currency exchange rate movements are recognized in earnings in the period in which the exchange rates change and offset the currency gains and losses on the underlying exposures being hedged. We perform an evaluation of the effectiveness of the hedge both at inception and on an ongoing basis. The ineffective portion of a hedge, if any, and changes in the fair value of a derivative not deemed to be a hedge, are recorded in the consolidated statement of operations.

We use interest rate swap agreements to hedge our exposure to variable rate debt and have designated these agreements as cash flow hedges of the forecasted interest payments. The fair values of the interest rate swap agreements are included in other assets for unrecognized gains and in other liabilities for unrecognized losses with an offset in accumulated other comprehensive items (net of tax).

We use forward currency-exchange contracts primarily to hedge certain operational (“cash flow” hedges) and balance sheet (“fair value” hedges) exposures resulting from fluctuations in currency exchange rates. Such exposures primarily result from portions of our operations and assets that are denominated in currencies other than the functional currencies of the businesses conducting the operations or holding the assets. As part of our overall strategy to manage the level of exposure to the risk of currency-exchange fluctuations, some of our subsidiaries hedge a portion of their currency exposures anticipated over the ensuing 12-month period, using forward currency-exchange contracts that have maturities of 12 months or less. We do not hold or engage in transactions involving derivative instruments for purposes other than risk management.

Valuation of Goodwill and Intangible Assets. We evaluate the recoverability of goodwill and indefinite-lived intangible assets annually in the fourth quarter, or more frequently if events or changes in circumstances, such as a decline in sales, earnings, or cash flows, or material adverse changes in the business climate, indicate that the carrying value of an asset might be impaired. Goodwill is considered to be impaired when the net book value of a reporting unit exceeds its estimated fair value. Fair values are primarily established using a discounted cash flow methodology (specifically, the income approach). The determination of discounted cash flows is based on our long-range forecasts. The revenue growth rates included in the forecasts are our best estimates based on current and anticipated market conditions, and the profit margin assumptions are projected based on current and anticipated cost structures. During the fourth quarter of 2008, we experienced a significant decline in our stock price. As a result of the decline in our stock price our market capitalization fell significantly below the recorded value of our consolidated net assets. The reduced market capitalization reflected, in part, the current economic climate, which has led, and we believe will continue to lead, to weakness in demand for some of our products. We completed the impairment test in the fourth quarter of 2008. The forecasts utilized in the impairment test reflected the anticipated decline in stock-preparation equipment sales, especially in China, which we expect to see over the next several years given the current economic environment and its impact on paper producers. The impairment test indicated the carrying amounts of goodwill for the stock-preparation reporting unit within our Papermaking Systems segment exceeded its implied fair value, and as a result, the Company recorded a $40.3 million pre-tax ($26.7 million after-tax) non-cash impairment charge to write down the goodwill associated with this reporting unit. The goodwill impairment test indicated that the estimated fair value of goodwill and indefinite-lived intangible assets associated with its other reporting units exceeded their carrying value and, as a result, no adjustment to goodwill was required for these reporting units. Intangible assets subject to amortization are evaluated for impairment if events or changes in circumstances indicate that the carrying value of an asset might be impaired. No adjustment was required in 2008 to the carrying value of our intangible assets subject to amortization based on the analysis performed.

Our judgments and assumptions regarding the determination of the fair value of an intangible asset or goodwill associated with an acquired business could change as future events impact such fair values. Any future impairment loss could have a material adverse affect on our long-term assets and operating expenses in the period in which an impairment is determined to exist.

Industry and Business Outlook

Our products are primarily sold to the global pulp and paper industry. The worldwide economic downturn, which accelerated in the fourth quarter of 2008, had a significant negative impact on paper producers. In response to the economic slowdown, paper producers took numerous steps to control operating costs including closing factories, increasing downtime at paper mills, and delaying or canceling projects. This slowdown was particularly pronounced in our stock-preparation equipment product line where we experienced a $37.6 million, or 23%, decrease in revenues in 2008 compared to 2007. The most significant factor contributing to this decrease was the slowdown in China, where the linerboard market is experiencing overcapacity. Our revenues from China are primarily derived from large capital orders, the timing of which is often difficult to predict. The recent downturn has caused many paper producers in China to significantly delay or even cancel projects. Slowdowns in financing approvals in China’s banking system have also negatively affected paper producers in the region. These delays, as well as delays in receiving down payments, could cause us to recognize revenue on these projects in periods later than originally anticipated. We expect our revenues in 2009, especially in our stock-preparation equipment product line, will continue to be negatively impacted by the current economic environment.

In response to this difficult environment, we have taken a number of steps to optimize our business structure and maximize internal efficiencies, which include integrating multiple operations in a region, merging our sales teams in certain markets, and reducing the number of employees in certain locations, including China and North America. In addition, we continue to concentrate our efforts on several initiatives intended to improve our operating results, including: increasing aftermarket sales, delivering products and technical solutions that provide our customers with a good return on their investments through energy-savings and fiber-yield improvements, penetrating existing markets where we see opportunity, and increasing our use of low-cost manufacturing bases. We also continue to focus our efforts on managing our operating costs, capital expenditures, and working capital.

For the first quarter of 2009, we expect to report a loss from continuing operations between $.03 and $.05 per diluted share, including $.07 of restructuring costs, on revenues of $62 to $65 million. For 2009, we expect to report income from continuing operations between $.43 to $.53 per diluted share, including $.17 of estimated restructuring costs, on revenues of $260 to $270 million.

Results of Operations

2008 Compared to 2007

The following table sets forth our consolidated statement of operations expressed as a percentage of total revenue:

	2008	2007
Revenues	100%	100%
Costs and Operating Expenses:		
Cost of revenues	59	62
Selling, general, and administrative expenses	30	26
Research and development expenses	2	2
Goodwill impairment	12	–
Restructuring costs (income) and other income, net	1	–
	104	90
Operating (Loss) Income	(4)	10
Interest Income	1	1
Interest Expense	(1)	(1)
(Loss) Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	(4)	10
Provision for Income Taxes	3	3
Minority Interest Expense	–	–
(Loss) Income from Continuing Operations	(7)	7
Income (Loss) from Discontinued Operation	–	(1)
Net (Loss) Income	(7)%	6%

Revenues

Revenues decreased $37.3 million, or 10%, to $329.2 million in 2008 from $366.5 million in 2007, including a $9.7 million increase from the favorable effects of currency translation. Excluding the effects of currency translation, revenues in 2008 decreased $47.0 million, or 13%, primarily due to a $43.1 million, or 26%, decrease in stock-preparation equipment sales. This significant decrease was due to a reduction in orders, especially in China and, to a lesser extent, North America, as major manufacturers cancelled or postponed projects due to the current economic environment. In addition, the decrease in revenues in 2008, excluding the effects of currency translation, included a $2.1 million, or 3%, decrease in our accessories product line and a $1.5 million decrease in our Casting Products business due to the sale of this business in April 2007.

Revenues for 2008 and 2007 for our Papermaking Systems segment and other businesses are as follows:

(In thousands)	2008	2007
Revenues:		
Papermaking Systems	$ 321,747	$ 356,334
Other Businesses	7,411	10,162
	$ 329,158	$ 366,496

Papermaking Systems Segment. Revenues at the Papermaking Systems segment decreased $34.6 million, or 10%, to $321.7 million in 2008 from $356.3 million in 2007, including a $9.7 million increase from the favorable effects of currency translation. Excluding the effects of currency translation, revenues in 2008 decreased $44.3 million, or 12%, primarily due to a $43.1 million, or 26%, decrease in our stock-preparation equipment sales.

Other Businesses. Revenues from our other businesses decreased $2.8 million, or 27%, to $7.4 million in 2008 from $10.2 million in 2007. Revenues from our Casting Products business decreased $1.5 million in 2008 due to its sale in April 2007. Revenues from the Fiber-based Products business decreased $1.3 million, or 15%, to $7.4 million in 2008 from $8.7 million in 2007 due to increased competition.

Papermaking Systems Segment By Product Line. The following table presents revenues at the Papermaking Systems segment by product line, the changes in revenues by product line between 2008 and 2007, and the changes in revenues by product line between 2008 and 2007 excluding the effect of currency translation. The presentation of the changes in revenues by product line, excluding the effect of currency translation, is a non-GAAP (generally accepted accounting principles) measure. We believe this non-GAAP measure helps investors gain a better understanding of our underlying operations, consistent with how management measures and forecasts our performance, especially when comparing such results to prior periods.

(In millions)	2008	2007	Increase (Decrease)	Increase (Decrease) Excluding Effect of Currency Translation
Papermaking Systems Product Lines:				
Stock-Preparation Equipment	$128.2	$165.8	$ (37.6)	$ (43.1)
Fluid-Handling	98.7	94.0	4.7	0.2
Accessories	60.7	63.1	(2.4)	(2.1)
Water-Management	31.7	31.1	0.6	0.6
Other	2.4	2.3	0.1	0.1
	$321.7	$356.3	$ (34.6)	$ (44.3)

Revenues from the segment's stock-preparation equipment product line decreased $37.6 million, or 23%, in 2008 compared to 2007, including a $5.5 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues in 2008 decreased $43.1 million, or 26%, primarily due to a $33.2 million, or 51%, decrease in stock-preparation equipment sales in China and a $17.9 million, or 28%, decrease in sales in North America. These significant decreases were due to a reduction in orders as major manufacturers cancelled or postponed projects due to the current economic environment. Offsetting the decreases in revenues in 2008, was an increase of $8.0 million, or 22%, in stock-preparation equipment sales in Europe due to several large projects. We expect to continue to see declines in stock-preparation equipment sales, especially in China, for the foreseeable future given the current economic environment and its impact on paper producers.

Revenues from the segment's fluid-handling product line increased $4.7 million, or 5%, in 2008 compared to 2007, including a $4.5 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues increased $0.2 million in 2008 due to stronger demand for our products in Europe and Southeast Asia and, to a lesser extent, Latin America. These increases were offset in part by a decrease in sales in North America and China.

Revenues from the segment's accessories product line decreased $2.4 million, or 4%, in 2008 compared to 2007, primarily due to decreased sales in North America and Europe.

Revenues from the segment's water-management product line increased $0.6 million, or 2%, in 2008 compared to 2007, due primarily to an increase in capital sales in North America.

Gross Profit Margin

Gross profit margin for 2008 and 2007 for our Papermaking Systems segment and our other businesses are as follows:

	2008	2007
Gross Profit Margin:		
Papermaking Systems	42%	38%
Other Businesses	27%	32%
	41%	38%

Gross profit margin increased to 41% in 2008 from 38% in 2007.

Papermaking Systems Segment. The gross profit margin at the Papermaking Systems segment increased to 42% in 2008 from 38% in 2007 primarily due to a more favorable product mix, which included a larger percentage of higher-margin aftermarket revenues, and the results of our ongoing efforts to shift our production and sourcing to lower cost countries.

Other Businesses. The gross profit margin at our other businesses decreased to 27% in 2008 from 32% in 2007 due to a decrease in revenues and an increase in the cost of natural gas. Natural gas prices have significantly decreased in the beginning of 2009 and as a result we expect improved results in this business in 2009.

Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues were 30% and 26% in 2008 and 2007, respectively. Selling, general, and administrative expenses increased $4.7 million, or 5%, to $100.3 million in 2008 from $95.6 million in 2007. This increase was primarily due to a $2.8 million unfavorable effect of currency translation, a $1.1 million increase in employee equity compensation expense from the grant of restricted stock units in March 2008 and May 2007, and $0.8 million in legal expenses attributable to litigation related to the composites business.

Total stock-based compensation expense was $2.9 million and $1.8 million in 2008 and 2007, respectively, and is included in selling, general, and administrative expenses. As of year-end 2008, unrecognized compensation expense related to restricted stock awards was approximately $3.5 million, which will be recognized over a weighted average period of 1.8 years.

Research and development expenses increased $0.2 million, or 4%, to $6.2 million in 2008 from $6.0 million in 2007 and represented 2% of revenues in both periods.

Goodwill Impairment

During 2008, we recorded a pre-tax goodwill impairment charge of $40.3 million ($26.7 million after-tax, or $1.98 per diluted share) associated with our stock-preparation reporting unit within the Papermaking Systems segment. We completed our annual goodwill impairment test in the fourth quarter of 2008 using the estimates from our long-range forecasts, which reflected the anticipated decline in stock-preparation equipment sales, especially in China, which we expect to see in the future given the current economic environment and its impact on paper producers. See *Valuation of Goodwill and Intangible Assets* in the *Application of Critical Accounting Policies and Estimates* in Item 7 for further discussion.

Restructuring Costs (Income) and Other Income, Net

During 2008, we recorded restructuring costs and other income, net of $2.0 million. The restructuring costs consisted of severance costs of $3.7 million related to the reduction of 329 full-time positions in China, Latin

America, Sweden, Canada, and the U.S. These actions were taken to adjust our cost structure and streamline our operations in response to the weak economic environment, which accelerated in the fourth quarter of 2008, and its negative impact on current and projected order volumes, especially in our stock-preparation equipment product line. We estimate annualized savings of $1.8 million in selling, general, and administrative expenses and $3.0 million in cost of revenues once these restructuring actions have been completed. We expect to record an additional $3.1 million of restructuring costs in 2009. Other income in 2008 consisted of a pre-tax gain of $1.1 million resulting from the sale of a building in the United Kingdom for $1.9 million in cash and a pre-tax gain of $0.6 million resulting from the sale of real estate in France for $0.7 million in cash. All of these items occurred in the Papermaking Systems segment.

During 2007, we recorded net restructuring income in our Papermaking Systems segment of $0.2 million, which included restructuring costs of $0.3 million related to exiting a facility and restructuring income of $0.5 million related to a reduction in the restructuring reserve as the reserve was no longer required.

Loss on Sale of Subsidiary

In April 2007, our Kadant Johnson Holdings Inc. (formerly Specialty Castings Inc.) subsidiary sold its Casting Products business for $0.4 million, resulting in a pre-tax loss of $0.4 million on the sale.

Interest Income

Interest income increased $0.3 million, or 23%, to $1.9 million in 2008 from $1.6 million in 2007 primarily due to higher average invested balances.

Interest Expense

Interest expense decreased $0.4 million, or 11%, to $2.7 million in 2008 from $3.1 million in 2007 primarily due to lower average borrowing rates.

Provision for Income Taxes

Our effective tax rate was (61%) and 28% in 2008 and 2007, respectively. The tax provision of $8.5 million, or (61%), in 2008, consisted of our 29% recurring tax rate and the following non-recurring items: a $15.4 million tax provision related to an increase in the valuation allowance on certain deferred tax assets, a $13.6 million tax benefit associated with the goodwill impairment charge, and a $1.0 million non-recurring tax benefit associated with our Canadian and Mexican operations. The 28% effective tax rate in 2007 consisted of our 30% recurring tax rate, offset by a 2% non-recurring tax benefit related to reductions in tax reserves largely as a result of the expiration of statues of limitation and return to provision true-up items mostly related to the U.S. tax cost of foreign earnings. We expect our effective tax rate to be between 33% and 34% in 2009.

(Loss) Income from Continuing Operations

We had a loss from continuing operations of $22.6 million in 2008 compared to income from continuing operations of $25.4 million in 2007. The loss from continuing operations in 2008 included a $40.3 million pre-tax goodwill impairment charge, a $15.4 million tax provision related to an increase in the valuation allowance on certain deferred tax assets, and a decrease in operating income, excluding goodwill impairment, of $9.7 million compared to 2007 (see *Revenues*, *Gross Profit Margin* and *Operating Expenses* discussed above).

Income (Loss) from Discontinued Operation

Income from the discontinued operation was $37 thousand in 2008 compared to a loss of $2.8 million in 2007 due primarily to a decrease of $3.9 million in pre-tax warranty costs.

As of January 3, 2009, the accrued warranty costs associated with the composites business were $2.1 million, which represents the low end of the estimated range of warranty reserve required based on the level of claims received through the end of 2008. Composites LLC has calculated that the total potential warranty cost ranges from $2.1 million to approximately $13.1 million. The high end of the range represents the estimated maximum level of warranty claims remaining based on the total sales of the products under warranty.

Composites LLC retained all of the cash proceeds received from the asset sale in October 2005 and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. Composites LLC will continue to record adjustments to accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments entered against it in litigation. Our consolidated results in future reporting periods will be negatively impacted if the future level of warranty claims exceed the warranty reserve.

Recent Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141(R) “Business Combinations” (SFAS 141(R)), which replaces SFAS No. 141. SFAS 141(R) requires the acquiring entity in a business combination to recognize the assets acquired and the liabilities assumed in the transaction, establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed, and requires the acquirer to disclose certain information to enable users to evaluate and understand the nature and financial effects of the business combination. SFAS 141(R) also requires that cash outflows, such as transaction costs and post-acquisition restructuring costs, be charged to expense instead of capitalized as a cost of the acquisition. Contingent purchase price will be recorded at its initial fair value and then re-measured as time passes through adjustments to net income. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. The adoption of SFAS 141(R) will have an impact on accounting for business combinations completed subsequent to its adoption and for certain transactions prior to adoption. As of January 3, 2009, we had a tax valuation allowance of $1.0 million relating to the Kadant Johnson Inc. acquisition, a liability for unrecognized tax benefits of $0.5 million, and accrued interest and penalties of $0.8 million, all of which would have affected goodwill if recognized prior to the end of fiscal 2008, but will now affect our annual effective tax rate if recognized.

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements—an Amendment of Accounting Research Bulletin No. 51” (SFAS 160), which establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent’s ownership interest and the valuation of retained non-controlling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners. SFAS 160 is effective for fiscal years beginning after December 15, 2008. We do not believe that the adoption of this statement will have a material affect on our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities” (SFAS 161). SFAS 161 requires disclosures of how and why an entity uses derivative instruments; how derivative instruments and related hedged items are accounted for; and how derivative instruments and related hedged items affect an entity’s financial position, financial performance and cash flows. SFAS 161 is effective for fiscal years beginning after November 15, 2008. The adoption of SFAS 161 will change our disclosures for derivative instruments and hedging activities beginning in the first quarter of 2009.

In April 2008, the FASB issued FASB Staff Position (FSP) FAS 142-3, “Determination of the Useful Life of Intangible Assets” (FSP FAS 142-3). FSP FAS 142-3 amends the factors that should be considered in developing the 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 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. We do not believe that the adoption of FSP FAS 142-3 will have a material affect on our consolidated financial statements.

In December 2008, the FASB issued FSP No. 132(R)-1, "Employers' Disclosures about Postretirement Benefit Plan Assets" (FSP 132(R)-1). FSP 132(R)-1 requires additional disclosures about an employer's plan assets of defined benefit pension or other postretirement plans. This rule expands current disclosures of defined benefit pension and postretirement plan assets to include information regarding the fair value measurements of plan assets similar to our current SFAS No. 157, "Fair Value Measurements", disclosures. FSP 132(R)-1 is effective for fiscal years ending after December 15, 2009. We are currently evaluating the potential impact of the adoption of FSP 132(R)-1 on our financial statement disclosures.

2007 Compared to 2006

The following table sets forth our consolidated statement of operations expressed as a percentage of total revenue:

	2007	2006
Revenues	100%	100%
Costs and Operating Expenses:		
Cost of revenues	62	63
Selling, general, and administrative expenses	26	26
Research and development expenses	2	2
Loss on sale of subsidiary	–	–
Restructuring costs and other income, net	–	–
	90	91
Operating Income	10	9
Interest Income	1	–
Interest Expense	(1)	(1)
Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	10	8
Provision for Income Taxes	3	3
Minority Interest Expense	–	–
Income from Continuing Operations	7	5
Loss from Discontinued Operation	(1)	–
Net Income	6%	5%

Revenues

Revenues increased $24.9 million, or 7%, to $366.5 million in 2007 from $341.6 million in 2006, including a $13.0 million increase from the favorable effects of currency translation. Excluding the effects of currency translation, revenues in 2007 increased primarily due to a $14.9 million, or 10%, increase from stock-preparation equipment sales due to higher capital equipment sales and a $4.6 million, or 5%, increase in our fluid-handling product line due in part to increased demand caused by higher energy prices. Offsetting these increases, excluding the favorable effects of currency translation, was a $3.4 million, or 10%, decrease in revenues in our water-management product line due to lower capital equipment sales, a $2.5 million, or 63%, decrease in revenues in our Casting Products business due to the sale of this business in April 2007, and a $1.4 million, or 14%, decrease in revenues in our Fiber-based Products business.

Revenues for 2007 and 2006 for our Papermaking Systems segment and other businesses are as follows:

(In thousands)	2007	2006
Revenues:		
Papermaking Systems	$ 356,334	$ 327,501
Other Businesses	10,162	14,112
	$ 366,496	$ 341,613

Papermaking Systems Segment. Revenues at the Papermaking Systems segment increased $28.8 million, or 9%, to $356.3 million in 2007 from $327.5 million in 2006. The increase in revenues in 2007 was primarily due to a $16.1 million, or 34%, increase in our stock-preparation equipment sales in North America and a $13.0 million increase from the favorable effects of currency translation.

Other Businesses. Revenues from our other businesses decreased $3.9 million, or 28%, to $10.2 million in 2007 from $14.1 million in 2006. Revenues from our Casting Products business decreased $2.5 million, or 63%, to $1.5 million in 2007 compared to $4.0 million in 2006 due to its sale in April 2007. Revenues from the Fiber-based Products business decreased $1.4 million, or 14%, to $8.7 million in 2007 from $10.1 million in 2006 due to increased competition which led to decreased sales of our fiber-based granules products sold under the tradename Biodac™.

Papermaking Systems Segment By Product Line. The following table presents revenues at the Papermaking Systems segment by product line, the changes in revenues by product line between 2007 and 2006, and the changes in revenues by product line between 2007 and 2006, excluding the effect of currency translation. The presentation of the changes in revenues by product line, excluding the effect of currency translation, is a non-GAAP (generally accepted accounting principles) measure. We believe this non-GAAP measure helps investors gain a better understanding of our underlying operations, consistent with how management measures and forecasts our performance, especially when comparing such results to prior periods.

(In millions)	2007	2006	Increase (Decrease)	Increase (Decrease) Excluding Effect of Currency Translation
Papermaking Systems Product Lines:				
Stock-Preparation Equipment	$165.8	$146.2	$ 19.6	$ 15.0
Fluid-Handling	94.0	84.4	9.6	4.6
Accessories	63.1	60.6	2.5	(0.2)
Water-Management	31.1	33.8	(2.7)	(3.4)
Other	2.3	2.5	(0.2)	(0.2)
	$356.3	$327.5	$ 28.8	$ 15.8

Revenues from the segment's stock-preparation equipment product line increased $19.6 million, or 13%, in 2007 compared to 2006, including a $4.6 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues in 2007 increased $15.0 million, or 10%, primarily due to a $16.1 million, or 34%, increase in sales of stock-preparation equipment in North America due to increased demand, offset, in part, by a $2.6 million decrease from sales in Europe.

Revenues from the segment's fluid-handling product line increased $9.6 million, or 11%, in 2007 compared to 2006, including a $5.0 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues increased $4.6 million, or 5%, in 2007 due in part to increased demand caused by higher energy prices.

Revenues from the segment's accessories product line increased $2.5 million, or 4%, in 2007 compared to 2006, including a $2.7 million increase from the favorable effect of currency transaction. Excluding the effect of currency translation, revenues decreased $0.2 million in 2007 compared to 2006.

Revenues from the segment's water-management product line decreased $2.7 million, or 8%, in 2007 compared to 2006, including a $0.7 million increase from the favorable effect of currency transaction. Excluding the effect of currency translation, revenues decreased $3.4 million, or 10%, in 2007 due primarily to a decrease in capital sales.

Gross Profit Margin

Gross profit margin for 2007 and 2006 for our Papermaking Systems segment and our other businesses are as follows:

	2007	2006
Gross Profit Margin:		
Papermaking Systems	38%	37%
Other Businesses	32%	28%
	38%	37%

Gross profit margin increased to 38% in 2007 from 37% in 2006.

Papermaking Systems Segment. The gross profit margin at the Papermaking Systems segment increased to 38% in 2007 from 37% in 2006.

Other Businesses. The gross profit margin at our other businesses increased to 32% in 2007 from 28% in 2006 due to the sale of our lower-margin Casting Products business in April 2007.

Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues were 26% in 2007 and 2006. Selling, general, and administrative expenses increased $5.4 million, or 6%, to $95.6 million in 2007 from $90.2 million in 2006. This increase was primarily due to a $3.5 million unfavorable effect of currency translation and a $0.9 million increase in stock-based compensation expense due primarily to the grant of restricted stock units in May 2007.

Research and development expenses decreased $0.2 million, or 4%, to $6.0 million in 2007 from $6.2 million in 2006 and represented 2% of revenues in both periods.

Total stock-based compensation expense was $1.8 million and $0.9 million in 2007 and 2006, respectively, and is included in selling, general, and administrative expenses. As of year-end 2007, unrecognized compensation cost related to stock options and restricted stock awards was approximately $4.4 million, which will be recognized over a weighted average period of 2.5 years.

Loss on Sale of Subsidiary

In April 2007, our Kadant Johnson Holdings Inc. (formerly Specialty Castings Inc.) subsidiary sold its Casting Products business for $0.4 million, resulting in a pre-tax loss of $0.4 million on the sale.

Restructuring Costs and Other Income, Net

During 2007, we recorded net restructuring income in our Papermaking Systems segment of $0.2 million, which included restructuring costs of $0.3 million related to exiting a facility and restructuring income of $0.5 million related to a reduction in the restructuring reserve as the reserve was no longer required.

During 2006, we recorded restructuring costs in our Papermaking Systems segment of $0.8 million, which included $0.7 million of severance and associated costs due to a reduction of 15 full-time employees in Canada and France and $0.1 million of equipment relocation costs associated with our 2005 restructuring actions.

Interest Income

Interest income increased $0.5 million, or 40%, to $1.6 million in 2007 from $1.1 million in 2006 primarily due to higher prevailing interest rates.

Interest Expense

Interest expense decreased $0.2 million, or 7%, to $3.1 million in 2007 from $3.3 million in 2006 primarily due to lower average outstanding borrowings as a result of a prepayment of $7.8 million of debt in May 2006.

Provision for Income Taxes

Our effective tax rate was 28% and 32% in 2007 and 2006, respectively. The 28% effective tax rate in 2007 consisted of our 30% recurring tax rate, offset by a 2% non-recurring tax benefit related to reductions in tax reserves largely as a result of the expiration of statues of limitation and return to provision true-up items mostly related to the U.S. tax cost of foreign earnings. The 32% effective tax rate in 2006 consisted of our 33% recurring tax rate, slightly offset by a 1% non-recurring tax benefit related to reductions in tax reserves associated with the favorable resolution of a state tax audit. We saw a 3% decrease in our recurring tax rate from 2006 to 2007 primarily due to a favorable geographical distribution of earnings and a reduction in nondeductible expenses.

Income from Continuing Operations

Income from continuing operations increased $7.1 million, or 39%, to $25.4 million in 2007 from $18.3 million in 2006. The increase in 2007 was primarily due to a $24.9 million, or 7%, increase in revenues which contributed to an increase in operating income of $7.6 million (see *Revenues*, *Gross Profit Margin* and *Operating Expenses* discussed above).

Loss from Discontinued Operation

The net loss from our discontinued operation increased $1.6 million, or 132%, to $2.8 million in 2007 from $1.2 million in 2006 due primarily to a $2.7 million pre-tax increase in warranty costs.

Liquidity and Capital Resources

Consolidated working capital was $98.0 million at January 3, 2009 compared with $107.5 million at December 29, 2007. Included in working capital are cash and cash equivalents of $40.1 million at January 3, 2009, compared with $61.6 million at December 29, 2007. At January 3, 2009, $37.0 million of cash and cash equivalents was held by our foreign subsidiaries.

2008

Our operating activities provided cash of $20.2 million in 2008 including $19.4 million provided by our continuing operations and $0.8 million provided by our discontinued operation. Contributing to the cash provided by continuing operations in 2008 was a decrease in unbilled contract costs and fees of $17.4 million as orders for our stock-preparation equipment decreased, especially in China and North America. Offsetting this source of cash was a decrease in accounts payable of $11.9 million and an increase in inventory of $10.2 million in 2008. The decrease in accounts payable and the increase in inventories primarily related to our stock-preparation equipment product line.

Our investing activities used cash of $5.3 million in 2008 related entirely to our continuing operations. We used $6.2 million of cash to purchase property, plant, and equipment. We also used $2.1 million of cash for additional consideration due on prior period acquisitions, including $1.2 million associated with the acquisition of Kadant Jining and $0.9 million associated with the acquisition of Kadant Johnson. Partially offsetting these uses of cash was $2.9 million of cash received from the sale of property, plant, and equipment.

Our financing activities used cash of $29.7 million in 2008 related entirely to our continuing operations. We used cash of $54.5 million in 2008 for principal payments on our debt obligations and $47.6 million to repurchase our common stock on the open market. These uses of cash were partially offset by $68.8 million of proceeds from the issuance of debt obligations and $3.8 million from the issuance of common stock in connection with the exercise of employee stock options.

2007

Our operating activities provided cash of $31.6 million in 2007, including $33.5 million provided by our continuing operations, offset by $1.9 million used by the discontinued operation. The cash provided by our continuing operations in 2007 was primarily due to income from continuing operations of $25.4 million, a non-cash charge of $7.4 million for depreciation and amortization expense, and a deferred tax provision of $5.9 million. Offsetting these sources of cash in 2007 was an increase in accounts receivable of $5.7 million and an increase in unbilled contract costs and fees of $3.2 million primarily associated with an increase in revenues in our stock-preparation equipment product line. The $1.9 million of cash used by the discontinued operation in 2007 was primarily related to the payment of $2.9 million for warranty claims.

Our investing activities used cash of $7.6 million in 2007, including $8.3 million used by continuing operations and $0.7 million provided by the discontinued operation. The cash used in continuing operations was primarily due to the purchase of $4.9 million of property, plant, and equipment. We also used $2.9 million of cash for additional consideration due on prior period acquisitions, including $2.2 million associated with the acquisition of Kadant Jining and $0.9 million associated with the acquisition of Kadant Johnson, offset in part by $0.2 million of cash received from the sale of our Casting Products business. The cash provided by the discontinued operation of $0.7 million relates to cash proceeds received in the first quarter of 2007 from the buyer of the assets of Composites LLC for post-closing adjustments.

Our financing activities used cash of $6.7 million in 2007 related entirely to our continuing operations. We used cash of $13.6 million in 2007 for principal payments on our debt obligations, including a $4.3 million prepayment in December 2007, and $5.2 million to repurchase our common stock on the open market. These uses of cash were partially offset by $9.2 million of proceeds from the issuance of common stock in connection with the exercise of employee stock options and $2.9 million of excess tax benefits from share-based payments.

Revolving Credit Facility

On February 13, 2008, we entered into a five-year unsecured revolving credit facility (2008 Credit Agreement) in the aggregate principal amount of up to $75 million, which includes an uncommitted unsecured incremental borrowing facility of up to an additional $75 million. We can borrow up to $75 million under the 2008 Credit Agreement with a sublimit of $60 million within the 2008 Credit Agreement available for the issuance of letters of credit and bank guarantees. The principal on any borrowings made under the 2008 Credit Agreement is due on February 13, 2013. Interest on any loans outstanding under the 2008 Credit Agreement accrues and is payable quarterly in arrears at one of the following rates selected by us: (a) the prime rate plus an applicable margin (up to .20%) or (b) a Eurocurrency rate plus an applicable margin (up to 1.20%). The applicable margin is determined based upon our total debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio. As of January 3, 2009, the outstanding balance borrowed under the 2008 Credit Agreement was $38.0 million. The amount we are able to borrow under the 2008 Credit Agreement is the total borrowing capacity less any outstanding borrowings, letters of credit and multi-currency borrowings issued under the 2008 Credit Agreement. As of January 3, 2009, we had $33.5 million of borrowing capacity available under the committed portion of the 2008 Credit Agreement.

Our obligations under the 2008 Credit Agreement may be accelerated upon the occurrence of an event of default under the 2008 Credit Agreement, which includes customary events of default including, without limitation, payment defaults, defaults in the performance of affirmative and negative covenants, the inaccuracy of representations or warranties, bankruptcy and insolvency related defaults, defaults relating to such matters as the Employment Retirement Income Security Act (ERISA), uninsured judgments and the failure to pay certain indebtedness, and a change of control default.

Borrowings under the 2008 Credit Agreement are guaranteed by certain of our domestic subsidiaries pursuant to the Guarantee Agreement effective as of February 13, 2008. In addition, the 2008 Credit Agreement contains negative covenants applicable to us and our subsidiaries, including financial covenants requiring us to comply with a maximum consolidated leverage ratio of 3.5 and a minimum consolidated fixed charge coverage ratio of 1.2, and restrictions on liens, indebtedness, fundamental changes, dispositions of property, making certain restricted payments (including dividends and stock repurchases), investments, transactions with affiliates, sale and leaseback transactions, swap agreements, changing our fiscal year, arrangements affecting subsidiary distributions, entering into new lines of business, and certain actions related to the discontinued operation. As of January 3, 2009, we were in compliance with these covenants.

Commercial Real Estate Loan

On May 4, 2006, we borrowed $10 million under a promissory note (2006 Commercial Real Estate Loan). The 2006 Commercial Real Estate Loan is repayable in quarterly installments of $125 thousand over a ten-year period with the remaining principal balance of $5 million due upon maturity. Interest on the 2006 Commercial Real Estate Loan accrues and is payable quarterly in arrears at one of the following rates selected by us (a) the prime rate or (b) the three-month London Inter-Bank Offered Rate (LIBOR) plus a 1% margin. Effective February 14, 2008, this margin was lowered to .75%. The 2006 Commercial Real Estate Loan is guaranteed and secured by real estate and related personal property of Kadant and certain of its domestic subsidiaries, located in Theodore, Alabama; Auburn, Massachusetts; Three Rivers, Michigan; and Queensbury, New York, pursuant to mortgage and security agreements dated May 4, 2006 (Mortgage and Security Agreements). As of January 3, 2009, the remaining balance on the 2006 Commercial Real Estate Loan was $8.8 million.

Our obligations under the 2006 Commercial Real Estate Loan may be accelerated upon the occurrence of an event of default under the 2006 Commercial Real Estate Loan and the Mortgage and Security Agreements, which includes customary events of default including without limitation payment defaults, defaults in the performance of covenants and obligations, the inaccuracy of representations or warranties, bankruptcy- and insolvency-related defaults, liens on the properties or collateral and uninsured judgments. In addition, the occurrence of an event of default under the 2008 Credit Agreement or any successor credit facility would be an event of default under the 2006 Commercial Real Estate Loan.

Kadant Jining Acquisition, Loans, and Credit Facilities

On June 2, 2006, our Kadant Jining subsidiary assumed responsibility for the operation of Huayi and, by September 30, 2006, acquired the assets of Huayi for approximately $21.2 million, net of assumed liabilities of $2.3 million. Of the total consideration, $17.3 million was paid in cash, including $1.0 million for acquisition-related costs. Of the remaining purchase obligation totaling $3.8 million, $3.6 million was paid as of January 3, 2009 and the remainder will be paid if certain indemnification obligations are satisfied.

To finance a portion of the acquisition, on June 6, 2006, Kadant Jining borrowed 40 million Chinese renminbi, or $5.9 million at the January 3, 2009 exchange rate, under a 47-month interest-only loan (2006 Kadant Jining Loan). The 2006 Kadant Jining Loan was repaid in January 2008.

On January 28, 2008, our Kadant Jining subsidiary borrowed 40 million Chinese renminbi, or approximately $5.9 million at the January 3, 2009 exchange rate (2008 Kadant Jining Loan). Principal on the 2008 Kadant Jining Loan is due as follows: 24 million Chinese renminbi, or approximately $3.5 million, on January 28, 2010 and 16 million Chinese renminbi, or approximately $2.4 million, on January 28, 2011. Interest on the 2008

Kadant Jining Loan accrues and is payable quarterly in arrears based on the interest rate published by The People's Bank of China for a loan of the same term less 5%. The proceeds from the 2008 Kadant Jining Loan were used to repay the 2006 Kadant Jining Loan totaling 40 million Chinese renminbi.

On July 30, 2008, Kadant Jining and our Kadant Yanzhou subsidiary (Kadant Yanzhou) each entered into a short-term credit line facility agreement (2008 Facilities) that would allow Kadant Jining to borrow up to an aggregate principal amount of 45 million Chinese renminbi, or approximately $6.6 million at the January 3, 2009 exchange rate, and Kadant Yanzhou to borrow up to an aggregate principal amount of 15 million Chinese renminbi, or approximately $2.2 million at the January 3, 2009 exchange rate. The 2008 Facilities have a term of 364 days and are renewable annually on or before July 30 at the discretion of the lender. Borrowings made under the 2008 Facilities will bear interest at the applicable short-term interest rate for a Chinese renminbi loan of comparable term as published by The People's Bank of China and will be used for general working capital purposes. We have provided a parent guaranty securing the payment of all obligations made under the Facilities and the 2008 Kadant Jining Loan and providing a cross-default to our other senior indebtedness, including the 2008 Credit Agreement. As of January 3, 2009, Kadant Jining had borrowed $2.8 million under the 2008 Facilities.

Interest Rate Swap Agreements

To hedge the exposure to movements in the 3-month LIBOR rate on outstanding debt, on February 13, 2008, we entered into a swap agreement (2008 Swap Agreement). The 2008 Swap Agreement has a five-year term and a $15 million notional value, which decreases to $10 million on December 31, 2010, and $5 million on December 30, 2011. Under the 2008 Swap Agreement, on a quarterly basis we will receive a 3-month LIBOR rate and pay a fixed rate of interest of 3.265%. We also entered into a swap agreement in 2006 (2006 Swap Agreement) to convert the 2006 Commercial Real Estate Loan from a floating to a fixed rate of interest. The 2006 Swap Agreement has the same terms and quarterly payment dates as the corresponding debt, and reduces proportionately in line with the amortization of the 2006 Commercial Real Estate Loan. Under the 2006 Swap Agreement, we will receive a three-month LIBOR rate and pay a fixed rate of interest of 5.63%. As of January 3, 2009, we hedged $23.8 million, or 43%, of our outstanding debt through interest rate swap agreements, which had an unrealized loss of $2.1 million. Our management believes that any credit risk associated with the 2006 and 2008 Swap Agreements is remote based on the creditworthiness of the financial institution issuing the swap agreements.

Additional Liquidity and Capital Resources

On May 5, 2008, our board of directors approved the repurchase by us of up to $30 million of our equity securities during the period from May 5, 2008 through May 5, 2009. We purchased 1,353,107 shares for $30.0 million in 2008 under this authorization. On October 22, 2008, our board of directors approved the repurchase by us of up to an additional $30 million of our equity securities during the period from October 22, 2008 through October 22, 2009. We purchased 204,693 shares for $3.0 million in 2008 and have $27.0 million remaining under this authorization. Repurchases under this authorization may be made in public or private transactions, including under Securities Exchange Act Rule 10b-5-1 trading plans.

It is our practice to reinvest indefinitely the earnings of our international subsidiaries, except in instances in which we can remit such earnings without a significant associated tax cost. Through January 3, 2009, we have not provided for U.S. income taxes on approximately $98.1 million of unremitted foreign earnings. The U.S. tax cost has not been determined due to the fact that it is not practicable to estimate at this time. The related foreign tax withholding, which would be required if we remitted the foreign earnings to the U.S., would be approximately $5.7 million.

It is our policy to provide for uncertain tax positions and the related interest and penalties based upon management's assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities. At January 3, 2009, we had a liability for unrecognized tax benefits and an accrual for the payment of interest and penalties totaling $6.5 million. To the extent we prevail in matters for which a liability for an unrecognized tax benefit is established or are required to pay amounts in excess of the liability, our effective tax rate in a given financial statement period may be affected.

In 2005, Composites LLC sold its composites business, presented as a discontinued operation in the accompanying consolidated financial statements. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including warranty obligations related to products manufactured prior to the sale date. Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. At January 3, 2009, the accrued warranty costs for Composites LLC were $2.1 million.

Although we currently have no material commitments for capital expenditures, we plan to make expenditures of approximately $4 to $5 million during 2009 for property, plant, and equipment.

In the future, our liquidity position will be primarily affected by the level of cash flows from operations, cash paid to satisfy debt repayments, capital projects, stock repurchases, or additional acquisitions, if any. We believe that our existing resources, together with the cash available from our credit facilities and the cash we expect to generate from continuing operations, will be sufficient to meet the capital requirements of our current operations for the foreseeable future.

Contractual Obligations and Other Commercial Commitments

The following table summarizes our known contractual obligations and commercial commitments to make future payments or other consideration pursuant to certain contracts as of January 3, 2009, as well as an estimate of the timing in which these obligations are expected to be satisfied. Detailed information concerning these obligations and commitments can be found in Notes 6 and 7 to our consolidated financial statements.

	Payments Due by Period or Expiration of Commitment				
(In millions)	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years	Total
Contractual Obligations and Other Commitments: (a)(b)					
Short- and long-term debt obligations	$ 3.3	$ 6.9	$ 39.0	$ 6.2	$ 55.4
Interest (c)	2.3	3.7	2.3	0.9	9.2
Operating lease obligations	2.0	2.4	1.0	–	5.4
Acquisition consideration (d)	0.9	2.5	–	–	3.4
Letters of credit (e)	15.6	5.2	–	–	20.8
Total (f)(g)	$ 24.1	$ 20.7	$ 42.3	$ 7.1	$ 94.2

(a) We have purchase obligations related to the acquisition of raw material made in the ordinary course of business that may be terminated with minimal notice and are excluded from this table.

(b) In the ordinary course of business, certain contracts contain limited performance guarantees, which do not require letters of credit, relating to our equipment and systems. We typically limit our liability under these guarantees to amounts that would not exceed the value of the contract. We believe that we have adequate reserves for any potential liability in connection with such guarantees. These guarantees are not included in this table.

(c) Amounts assume interest rates on variable rate debt remain unchanged from rates as of January 3, 2009.

(d) In addition to the consideration paid at closing for Kadant Johnson, $3.4 million will be paid through 2010 related to certain tax assets of Kadant Johnson, the value of which we expect to realize.

(e) Primarily relates to performance obligations and customer deposit guarantees. This total excludes letters of credit of $3.4 million, which guarantee payment of amounts accrued on the balance sheet and are reflected in the table within acquisition consideration. Typically, these performance obligations and customer deposit guarantees have expired without being drawn upon.

(f) This table excludes $2.9 million of accrued restructuring costs, of which $2.3 million will be paid in 2009 and $0.6 million will be paid from 2010 to 2015. In addition, the table excludes $11.7 million of accrued pension and other post-retirement benefits as these liabilities are not subject to fixed payment terms.

(g) This table excludes a liability for unrecognized tax benefits and an accrual for the payment of interest and penalties totaling $6.5 million. Due to the uncertain nature of these tax matters, we are unable to make a reasonably reliable estimate as to if and when cash settlements with the appropriate taxing authorities will occur.

Provisions in financial guarantees or commitments, debt or lease agreements, or other arrangements could trigger a requirement for an early payment, additional collateral support, amended terms, or acceleration of maturity.

We do not have special-purpose entities nor do we use off-balance-sheet financing arrangements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk from changes in interest rates and foreign currency exchange rates, which could affect our future results of operations and financial condition. We manage our exposure to these risks through our regular operating and financing activities. We entered into "receive-variable pay-fixed" swap agreements in 2006 and 2008 to hedge our exposure to variable rate long-term debt. Additionally, we use short-term forward contracts to manage certain exposures to foreign currencies. We enter into forward currency-exchange contracts to hedge firm purchase and sale commitments denominated in currencies other than our subsidiaries' local currencies. We do not engage in extensive foreign currency hedging activities; however, the purpose of our foreign currency hedging activities is to protect our local currency cash flows related to these commitments from fluctuations in foreign exchange rates. Our forward currency-exchange contracts principally hedge transactions denominated in U.S. dollars. Gains and losses arising from forward contracts are recognized as offsets to gains and losses resulting from the transactions being hedged. We do not use financial instruments for trading purposes.

Interest Rates

Our cash and cash equivalents are sensitive to changes in interest rates. Interest rate changes would result in a change in interest income due to the difference between the current interest rates on cash and cash equivalents and the variable rates to which these financial instruments may adjust in the future. A 10% decrease in year-end interest rates would have resulted in a negative impact on our net income of $0.1 million in both 2008 and 2007.

A portion of our outstanding debt is sensitive to changes in interest rates. We hedged $23.8 million and $30.9 million of our debt at year-end 2008 and 2007, respectively, with "receive-variable pay-fixed" swap agreements. The fair values of the swap agreements are sensitive to changes in long-term swap rates. A 10% decrease in the long-term swap rates would have resulted in an increase in unrealized losses of $0.4 million and $0.3 million as of year-end 2008 and 2007, respectively. The remaining unhedged portion of the debt totaling $31.6 million and $9.8 million as of year-end 2008 and 2007, respectively, is sensitive to changes in interest rates. As of year-end 2008 and 2007, the interest rate on the unhedged portion of our U.S. debt was based on LIBOR, and for our foreign debt, based on rates established by The People's Bank of China. A 10% increase in the year-end rates would have resulted in a negative impact on our net (loss) income of $0.1 million in both 2008 and 2007.

Currency Exchange Rates

We generally view our investment in foreign subsidiaries in a functional currency other than our reporting currency as long-term. Our investment in foreign subsidiaries is sensitive to fluctuations in foreign currency exchange rates. The functional currencies of our foreign subsidiaries are principally denominated in euros, British pounds sterling, Mexican pesos, Canadian dollars, Chinese renminbi and Brazilian reals. The effect of changes in foreign exchange rates on our net investment in foreign subsidiaries is reflected in the "accumulated other comprehensive items" component of shareholders' investment. A 10% depreciation in functional currencies at year-end 2008 and 2007, relative to the U.S. dollar, would have resulted in a reduction in shareholders' investment of $17.7 million and $16.6 million, respectively.

The fair value of forward currency-exchange contracts is sensitive to fluctuations in foreign currency exchange rates. The fair value of forward currency-exchange contracts is the estimated amount that we would pay or receive upon termination of the contracts, taking into account the change in foreign currency exchange rates. A 10% depreciation in year-end 2008 and 2007 foreign currency exchange rates related to our contracts would have resulted in an increase in unrealized losses on forward currency-exchange contracts of $3.1 million and $1.5 million in 2008 and 2007, respectively. Since we use forward currency-exchange contracts as hedges of firm purchase and sale commitments, the unrealized gain or loss on forward foreign currency-exchange contracts resulting from changes in foreign currency exchange rates would be offset primarily by corresponding changes in the fair value of the hedged items.

Item 8. Financial Statements and Supplementary Data

This data is submitted as a separate section to this Report. See Item 15, "Exhibits and Financial Statement Schedules."

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

Not applicable.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of January 3, 2009. The term "disclosure controls and procedures," as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based upon the evaluation of our disclosure controls and procedures as of January 3, 2009, our Chief Executive Officer and Chief Financial Officer concluded that as of January 3, 2009, our disclosure controls and procedures were effective at the reasonable assurance level.

Evaluation of Changes in Internal Controls over Financial Reporting

There have not been any changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the fiscal quarter ended January 3, 2009 that have materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Securities Exchange Act Rules 13a-15(f) and 15d-15(f). Our management assessed the effectiveness of our internal control over financial reporting as of January 3, 2009. In making this assessment, our management used the criteria set forth in "Internal Control—Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment, management believes that, as of January 3, 2009 our internal control over financial reporting is effective based on the criteria issued by COSO.

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

Our independent registered public accountants, Ernst & Young LLP, have issued an audit report on our internal control over financial reporting, which is included herein on page F-3 and incorporated into this Item 9A by reference.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers, and Corporate Governance

This information will be under the heading "Election of Directors" in our 2009 proxy statement for our 2009 Annual Meeting of Shareholders and is incorporated in this Report by reference, except as follows. The information concerning executive officers is included under the heading "Executive Officers of the Registrant" in Item 1 of Part I of this Report.

Section 16(a) Beneficial Ownership Reporting Compliance

The information required under Item 405 of Regulation S-K is included under the heading "Stock Ownership–Section 16(a) Beneficial Ownership Reporting Compliance" in our 2009 proxy statement and is incorporated in this Report by reference.

Corporate Governance

The information required under Item 406 of Regulation S-K will be included under the heading "Election of Directors—Corporate Governance—Code of Business Conduct and Ethics" in our 2009 proxy statement and is incorporated in this Report by reference.

Item 11. Executive Compensation

This information will be included under the headings "Executive Compensation", "Compensation Committee Interlocks and Insider Participation", and "Compensation Committee Report" in our 2009 proxy statement and is incorporated in this Report by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Except for the information concerning equity compensation plans, this information will be included under the heading "Stock Ownership" in our 2009 proxy statement and is incorporated in this Report by reference.

The following table provides information about the securities authorized for issuance under our equity compensation plans as of January 3, 2009:

Equity Compensation Plan Information

Plan Category	(a) Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants, and Rights	(b) Weighted-Average Exercise Price of Outstanding Options, Warrants, and Rights	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Equity compensation plans approved by security holders	369,274(1)	$ 30.52(1)	1,002,237(2)
Equity compensation plans not approved by security holders (3)	9,167	$ 19.76	23,902
Total	378,441(1)	$ 30.26(1)	1,026,139(2)

(1) Excludes an aggregate of 197,488 shares of common stock issuable under our employees' stock purchase plan in connection with current and future offering periods under the plan. Excludes 2,569 shares reserved for issuance pursuant to our deferred compensation plan for directors.

(2) Includes 197,488 shares of common stock issuable under our employees' stock purchase plan in connection with current and future offering periods under the plan. Excludes 2,569 shares reserved for issuance pursuant to our deferred compensation plan for directors.

(3) The material features of our 2001 employee equity incentive plan are described in Part IV, Item 15, Exhibits and Financial Statement Schedules, Note 3 to the audited consolidated financial statements of this Report.

Item 13. Certain Relationships and Related Transactions, and Director Independence

This information will be included under the heading "Election of Directors" in our 2009 proxy statement and is incorporated in this Report by reference.

Item 14. Principal Accountant Fees and Services

This information will be included under the heading "Independent Registered Public Accounting Firm" in our 2009 proxy statement and is incorporated in this Report by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) The following documents are filed as part of this Report:

(1) Consolidated Financial Statements (see Index on Page F-1 of this Report):

Report of Independent Registered Public Accounting Firm on Consolidated Financial Statements and Schedule

Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting

Consolidated Statement of Operations

Consolidated Balance Sheet

Consolidated Statement of Cash Flows

Consolidated Statement of Comprehensive (Loss) Income and Shareholders' Investment

Notes to Consolidated Financial Statements

(2) Consolidated Financial Statement Schedule (see Index on Page F-1 of this Report):

Schedule II: Valuation and Qualifying Accounts

All other schedules are omitted because they are not applicable or not required, or because the required information is shown either in the consolidated financial statements or in the notes thereto.

(3) Exhibits filed herewith or incorporated in this Report by reference are set forth in the Exhibit Index beginning on page 45. This list of exhibits identifies each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Report.

(b) Exhibits

See the Exhibit Index beginning on page 45.

Signatures

Pursuant to the requirements of Section 13 or 15(d) 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.

Date: March 9, 2009

KADANT INC.

By: /S/ WILLIAM A. RAINVILLE
William A. Rainville
Chairman of the Board, Chief Executive Officer, and President

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated, on March 9, 2009.

Signature	Title
By: /S/ WILLIAM A. RAINVILLE **William A. Rainville**	Chairman of the Board, Chief Executive Officer, and President
By: /S/ THOMAS M. O'BRIEN **Thomas M. O'Brien**	Executive Vice President, Chief Financial Officer
By: /S/ MICHAEL J. MCKENNEY **Michael J. McKenney**	Vice President, Finance and Chief Accounting Officer
By: /S/ JOHN M. ALBERTINE **John M. Albertine**	Director
By: /S/ JOHN K. ALLEN **John K. Allen**	Director
By: /S/ THOMAS C. LEONARD **Thomas C. Leonard**	Director
By: /S/ FRANCIS L. MCKONE **Francis L. McKone**	Director

Table of Contents

Exhibit Index

Exhibit Number	Description of Exhibit
2.1	Purchase Agreement among the Registrant, Johnson Acquisition Corp., The Johnson Corporation and the principal shareholders of Johnson identified in the Purchase Agreement (filed as Exhibit 99.2 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on April 12, 2005 and incorporated in this document by reference). (1)
2.2	Purchase Agreement dated October 21, 2005, among the Registrant, its Kadant Composites LLC subsidiary, LDI Composites Co., a Minnesota corporation, and Liberty Diversified Industries, Inc., a Minnesota corporation, and parent corporation of the Buyer (filed as Exhibit 99.1 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on October 27, 2005 and incorporated in this document by reference). (1)
2.3	First Amendment dated as of October 10, 2006 to the Asset Purchase Agreement dated as of October 21, 2005, among the Registrant, its Kadant Composites LLC subsidiary, LDI Composites Co., a Minnesota corporation, and Liberty Diversified Industries, Inc., a Minnesota corporation, and parent corporation of the Buyer (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 29, 2007 [File No. 1-11406] and incorporated in this document by reference).
3.1	Restated Certificate of Incorporation of the Registrant (filed as Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001 [File No. 1-11406] and incorporated in this document by reference).
3.2	Amended and Restated Bylaws of the Registrant (filed as Exhibit 3.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001 [File No. 1-11406] and incorporated in this document by reference).
4.1	Rights Agreement, dated as of July 16, 2001, between the Registrant and American Stock Transfer & Trust Company, which includes as Exhibit A the Form of Certificate of Designations, as Exhibit B the Form of Rights Certificate, and as Exhibit C the Summary of Rights to Purchase Preferred Stock (filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on July 17, 2001, and incorporated in this document by reference).
10.1*	Form of Indemnification Agreement between the Registrant and its directors and officers (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001 [File No. 1-11406] and incorporated in this document by reference).
10.2*	Amended and Restated Executive Retention Agreement (change in control agreement) between the Company and Mr. William A. Rainville, chairman and chief executive officer of the Company, dated as of December 9, 2008.
10.3*	Form of Amended and Restated Executive Retention Agreement (change in control agreement) between the Company and Other Senior Officers, as amended and restated on December 9, 2008.
10.4*	Amended and Restated Nonqualified Stock Option Plan of the Registrant.
10.5*	Amended and Restated Equity Incentive Plan of the Registrant.
10.6*	2001 Employees Equity Incentive Plan of the Registrant.
10.7*	Kadant Inc. 2006 Equity Incentive Plan.
10.8*	Amended and Restated Deferred Compensation Plan for Directors of the Registrant (filed as Exhibit 10.5 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended July 3, 1999 [File No. 1-11406] and incorporated in this document by reference).

Table of Contents

Exhibit Number	Description of Exhibit
10.9*	Amended and Restated Directors' Restricted Stock Plan (filed as Exhibit 10.10 to the Registrant's Annual Report on Form 10-K for the year ended January 3, 2004 [File No. 1-11406] and incorporated in this document by reference).
10.10*	Cash Incentive Plan of the Registrant.
10.11*	Summary of Non-employee Director Compensation of the Registrant (filed as Exhibit 10.11 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2007 [File No. 1-11406] and incorporated in this document by reference).
10.12*	Form of Restricted Stock Agreement for award of restricted shares to non-employee directors used for restricted stock awards on and after February 27, 2007 (filed as Exhibit 10.13 to the Registrant's Annual Report on Form 10-K for the year ended December 30, 2006 [File No. 1-11406] and incorporated in this document by reference).
10.13*	Form of Performance-Based Restricted Stock Unit Award Agreement dated May 24, 2007 between the Company and its executive officers (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 [File No. 1-11406] and incorporated in this document by reference).
10.14*	Form of Performance-Based Restricted Stock Unit Award Agreement dated March 3, 2008 between the Company and its executive officers (filed as Exhibit 10.15 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2007 [File No. 1-11406] incorporated in this document by reference).
10.15*	Form of First Amendment to Performance-Based Restricted Stock Unit Award Agreement dated December 9, 2008 between the Company and its executive officers with respect to awards granted prior to December 9, 2008.
10.16*	Form of Performance-Based Restricted Stock Unit Award Agreement between the Company and its executive officers used for restricted stock unit awards on and after December 9, 2008.
10.17*	Form of Restricted Stock Unit Award Agreement dated March 3, 2008 between the Company and its non-employee directors (filed as Exhibit 10.15 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2007 [File No. 1-11406] incorporated in this document by reference).
10.18*	Form of First Amendment to Restricted Stock Unit Award Agreement between the Company and its non-employee directors with respect to awards granted prior to December 9, 2008.
10.19*	Form of Restricted Stock Unit Award Agreement between the Company and its non-employee directors used for restricted stock unit awards on and after December 9, 2008.
10.20	Credit Agreement dated February 13, 2008 among the Registrant, the Foreign Subsidiary Borrowers from time to time parties thereto, the several banks and other financial institutions or entities from time to time parties thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent, and J.P. Morgan Europe Limited, as Multi-currency Administrative Agent (filed as Exhibit 99.1 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on February 15, 2008 and incorporated in this document by reference). (1)

Exhibit Index

Exhibit Number	Description of Exhibit
10.21	Guarantee Agreement dated February 13, 2008, among Kadant Inc. and the Subsidiary Guarantors, in favor of JPMorgan Chase Bank, N.A., as Administrative Agent for the several banks and other financial institutions or entities from time to time parties to the Credit Agreement dated as of February 13, 2008 (filed as Exhibit 99.2 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on February 15, 2008 and incorporated in this document by reference). (1)
10.22	Joinder Agreement dated as of March 17, 2008, to Credit Agreement dated as of February 13, 2008, among the Registrant, the Foreign Subsidiary Borrowers from time to time parties thereto, the several lenders from time to time parties thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent, and J.P. Morgan Europe Limited, as Multi-currency Administrative Agent (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 29, 2008 [File No. 1-11406] and incorporated in this document by reference).
10.23	International Swap Dealers Association, Inc. Master Agreement dated May 13, 2005 between the Registrant and Citizens Bank of Massachusetts and Swap Confirmation dated May 18, 2005 (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended July 2, 2005 [File No. 1-11406] and incorporated in this document by reference).
10.24	Swap Confirmation dated February 13, 2008 between the Registrant and RBS Citizens, N.A. (filed as Exhibit 10.35 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2007 [File No. 1-11406] and incorporated in this document by reference).
10.25	Promissory Note in the principal amount of $10,000,000 dated May 4, 2006, between Kadant and Citizens Bank of Massachusetts (filed as Exhibit 99.1 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference).
10.26	Limited Guaranty Agreement dated May 4, 2006 between Kadant Web Systems Inc., a Massachusetts corporation, and Citizens Bank of Massachusetts (filed as Exhibit 99.2 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference).
10.27	Limited Guaranty Agreement dated May 4, 2006 between Kadant Black Clawson Inc., a Delaware corporation, and Citizens Bank of Massachusetts (filed as Exhibit 99.3 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference).
10.28	Limited Guaranty Agreement dated May 4, 2006 between Kadant Johnson Inc., a Michigan corporation, and Citizens Bank of Massachusetts (filed as Exhibit 99.4 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference).
10.29	Mortgage and Security Agreement dated May 4, 2006 between Kadant and Citizens Bank of Massachusetts relating to the real property and related personal property located in Queensbury, New York (filed as Exhibit 99.5 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference). (1)
10.30	Mortgage and Security Agreement dated May 4, 2006 between Kadant Web Systems Inc., a Massachusetts corporation, and Citizens Bank of Massachusetts relating to the real property and related personal property located in Auburn, Massachusetts (filed as Exhibit 99.6 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference). (1)

Exhibit Number	Description of Exhibit
10.31	Mortgage and Security Agreement dated May 4, 2006 between Kadant Black Clawson Inc., a Delaware corporation, and Citizens Bank of Massachusetts relating to the real property and related personal property located in Theodore, Alabama (filed as Exhibit 99.7 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference). (1)
10.32	Mortgage and Security Agreement dated May 9, 2006 between Kadant Johnson Inc., a Michigan corporation, and Citizens Bank of Massachusetts relating to the real property and related personal property located in Three Rivers, Michigan (filed as Exhibit 99.8 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on May 9, 2006 and incorporated in this document by reference). (1)
10.33	Guaranty Agreement dated as of July 30, 2007 between the Registrant and JPMorgan Chase Bank, N.A., Shanghai Branch (filed as Exhibit 10.4 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 [File No. 1-11406] and incorporated in this document by reference).
10.34	Amendment, Acknowledgement and Consent to the Guaranty dated as of January 28, 2008 to the Guaranty Agreement dated as of July 30, 2007 of the Registrant in favor of JPMorgan Chase Bank, N.A., Shanghai Branch (filed as Exhibit 10.34 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2007 [File No. 1-11406] and incorporated in this document by reference).
10.35	Second Amendment to the Guaranty Agreement dated as of July 30, 2008 between the Registrant and JPMorgan Chase Bank, N.A., Shanghai Branch (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 28, 2008 [File No. 1-11406] and incorporated in this document by reference).
10.36	RMB 40,000,000 Term Loan Agreement dated as of January 28, 2008 between Kadant Light Machinery (Jining) Co., Ltd. and JPMorgan Chase Bank (China) Company Limited, Shanghai Branch (filed as Exhibit 99 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on February 1, 2008, and incorporated in this document by reference).
10.37	Plan and Agreement of Distribution, dated as of August 3, 2001, between the Registrant and Thermo Electron Corporation (filed as Exhibit 99.3 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on August 6, 2001, and incorporated in this document by reference).
10.38	First Amendment to Plan and Agreement of Distribution, dated as of December 27, 2001, between the Registrant and Thermo Electron Corporation (filed as Exhibit 10.4 to the Registrant's Annual Report on Form 10-K for the year ended December 29, 2001 [File No. 1-11406] and incorporated in this document by reference).
10.39	Tax Matters Agreement, dated as of August 8, 2001, between the Registrant and Thermo Electron Corporation (filed as Exhibit 99.4 to the Registrant's Current Report on Form 8-K [File No. 1-11406] filed with the Commission on August 6, 2001, and incorporated in this document by reference).
21	Subsidiaries of the Registrant.
23.1	Consent of Independent Registered Public Accounting Firm.
31.1	Certification of the Principal Executive Officer of the Registrant Pursuant to Rule 13a-15(e) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.

Table of Contents

Exhibit Number	Description of Exhibit
31.2	Certification of the Principal Financial Officer of the Registrant Pursuant to Rule 13a-15(e) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
32	Certification of the Chief Executive Officer and the Chief Financial Officer of the Registrant pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Management contract or compensatory plan or arrangement.

(1) The schedules to this document have been omitted from this filing pursuant to Item 601(b)(2) of Regulation S-K. The Company will furnish copies of any of the schedules to the U.S. Securities and Exchange Commission upon request.

Exhibit Index

[Table of Contents](#)

Kadant Inc.
Annual Report on Form 10-K
Index to Consolidated Financial Statements and Schedule

The following Consolidated Financial Statements of the Registrant and its subsidiaries are required to be included in Item 8:

The following Consolidated Financial Statement Schedule of the Registrant and its subsidiaries is filed as part of this Report as required to be included in Item 15(a)(2):

Report of Independent Registered Public Accounting Firm
on Consolidated Financial Statements and Schedule

To the Board of Directors and Shareholders of Kadant Inc.:

We have audited the accompanying consolidated balance sheets of Kadant Inc. as of January 3, 2009 and December 29, 2007, and the related consolidated statements of operations, comprehensive (loss) income and shareholders' investment, and cash flows for each of the three fiscal years in the period ended January 3, 2009. Our audits also included the financial statement schedule listed in the index at Item 15(a)(2). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Kadant Inc. at January 3, 2009 and December 29, 2007 and the consolidated results of their operations and their cash flows for each of the three years in the fiscal period ended January 3, 2009, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, effective December 31, 2006, Kadant Inc. adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109* and as discussed in Note 3 to the consolidated financial statements, effective December 30, 2006, Kadant Inc. adopted Statement of Financial Accounting Standards No. 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans, an Amendment of FASB Statements No. 87, 88, 106 and 132(R)* and effective January 1, 2006, Kadant Inc. adopted Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment*.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Kadant Inc.'s internal control over financial reporting as of January 3, 2009, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 3, 2009 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 3, 2009

Report of Independent Registered Public Accounting Firm
on Internal Control over Financial Reporting

To the Board of Directors and Shareholders of Kadant Inc.:

We have audited Kadant Inc.'s internal control over financial reporting as of January 3, 2009, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Kadant Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

In our opinion, Kadant Inc. maintained, in all material respects, effective internal control over financial reporting as of January 3, 2009, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the 2008 consolidated financial statements of Kadant Inc. and our report dated March 3, 2009 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 3, 2009

Table of Contents

Consolidated Statement of Operations

(In thousands, except per share amounts)	2008	2007	2006
Revenues (Note 11)	$329,158	$366,496	$341,613
Costs and Operating Expenses:			
Cost of revenues	193,355	227,716	214,919
Selling, general, and administrative expenses	100,280	95,616	90,236
Research and development expenses	6,187	5,957	6,201
Goodwill impairment (Note 1)	40,333	–	–
Restructuring costs (income) and other income, net (Note 8)	2,010	(219)	815
Loss on sale of subsidiary (Note 2)	–	388	–
	342,165	329,458	312,171
Operating (Loss) Income	(13,007)	37,038	29,442
Interest Income	1,935	1,570	1,121
Interest Expense (Note 6)	(2,738)	(3,086)	(3,328)
(Loss) Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	(13,810)	35,522	27,235
Provision for Income Taxes (Note 5)	8,466	9,784	8,688
Minority Interest Expense	319	320	266
(Loss) Income from Continuing Operations	(22,595)	25,418	18,281
Income (Loss) from Discontinued Operation (net of income tax benefit of $65, $1,508 and $702 in 2008, 2007, and 2006, respectively; Note 9)	37	(2,750)	(1,184)
Net (Loss) Income	$ (22,558)	$ 22,668	$ 17,097
(Loss) Earnings per Share from Continuing Operations (Note 12)			
Basic	$ (1.67)	$ 1.80	$ 1.32
Diluted	$ (1.67)	$ 1.78	$ 1.30
(Loss) Earnings per Share (Note 12)			
Basic	$ (1.67)	$ 1.61	$ 1.24
Diluted	$ (1.67)	$ 1.59	$ 1.21
Weighted Average Shares (Note 12)			
Basic	13,527	14,116	13,816
Diluted	13,527	14,290	14,097

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

Consolidated Balance Sheet

(In thousands, except share amounts)	2008	2007
Assets		
Current Assets:		
Cash and cash equivalents	$ 40,139	$ 61,553
Accounts receivable, less allowances of $2,985 and $2,639	54,517	58,404
Unbilled contract costs and fees	9,631	27,487
Inventories	55,762	47,470
Other current assets	16,434	11,046
Assets of discontinued operation (Note 9)	524	1,293
Total Current Assets	177,007	207,253
Property, Plant, and Equipment, at Cost, Net	41,638	41,904
Other Assets	13,127	14,156
Intangible Assets	30,115	32,944
Goodwill (Note 1)	95,030	140,812
Total Assets	$356,917	$437,069
Liabilities and Shareholders' Investment		
Current Liabilities:		
Short-term obligations and current maturities of long-term obligations (Note 6)	$ 3,289	$ 10,240
Accounts payable	24,212	37,132
Accrued payroll and employee benefits	14,475	17,510
Customer deposits	11,747	12,956
Other current liabilities	22,840	19,500
Liabilities of discontinued operation (Note 9)	2,427	2,428
Total Current Liabilities	78,990	99,766
Deferred Income Taxes (Note 5)	10,322	8,899
Other Long-Term Liabilities (Note 3)	21,090	17,731
Long-Term Obligations (Note 6)	52,122	30,460
Minority Interest	1,678	1,462
Commitments and Contingencies (Note 7)		
Shareholders' Investment (Notes 3 and 4):		
Preferred stock, $.01 par value, 5,000,000 shares authorized; none issued	–	–
Common stock, $.01 par value, 150,000,000 shares authorized; 14,624,159 and 14,604,520 shares issued	146	146
Capital in excess of par value	92,916	91,753
Retained earnings	152,548	175,106
Treasury stock at cost, 2,074,362 and 174,045 shares	(46,707)	(4,152)
Accumulated other comprehensive items (Note 13)	(6,188)	15,898
Total Shareholders' Investment	192,715	278,751
Total Liabilities and Shareholders' Investment	$356,917	$437,069

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

Consolidated Statement of Cash Flows

(In thousands)	2008	2007	2006
Operating Activities			
Net (loss) income	$(22,558)	$ 22,668	$ 17,097
(Income) loss from discontinued operation (Note 9)	(37)	2,750	1,184
(Loss) income from continuing operations	(22,595)	25,418	18,281
Adjustments to reconcile (loss) income from continuing operations to net cash provided by operating activities:			
Goodwill impairment	40,333	–	–
Depreciation and amortization	7,530	7,363	7,758
Stock-based compensation expense	2,945	1,796	926
(Gain) loss on sale of property, plant and equipment	(1,761)	20	–
Provision for losses on accounts receivable	1,252	216	725
Minority interest expense	319	320	266
Deferred income tax expense	4,051	4,930	5,065
Other items, net	(790)	(1,716)	(1,403)
Changes in current accounts, net of effects of acquisitions and disposition:			
Accounts receivable	(220)	(5,657)	(6,941)
Unbilled contract costs and fees	17,412	(3,213)	(12,137)
Inventories	(10,202)	(3,827)	(3,126)
Other current assets	(1,387)	(923)	22
Accounts payable	(11,900)	2,806	11,280
Other current liabilities	(5,629)	5,976	(8,383)
Net cash provided by continuing operations	19,358	33,509	12,333
Net cash provided by (used in) discontinued operation	803	(1,866)	(4,172)
Net cash provided by operating activities	20,161	31,643	8,161
Investing Activities			
Acquisitions and disposition, net of cash acquired	(2,119)	(2,867)	(18,340)
Purchases of property, plant, and equipment	(6,198)	(4,908)	(4,097)
Proceeds from sale of property, plant, and equipment	2,859	157	412
Other, net	155	(633)	(316)
Net cash used in continuing operations	(5,303)	(8,251)	(22,341)
Net cash provided by discontinued operation	–	660	4,271
Net cash used in investing activities	(5,303)	(7,591)	(18,070)
Financing Activities			
Proceeds from issuance of short- and long-term obligations	68,791	–	15,124
Repayment of short- and long-term obligations	(54,474)	(13,633)	(16,642)
Purchases of Company common stock	(47,623)	(5,185)	(7,181)
Proceeds from issuance of Company common stock	3,825	9,225	9,380
Excess tax benefits from stock option exercises	532	2,946	2,529
Other, net	(766)	(25)	(173)
Net cash (used in) provided by continuing operations in financing activities	(29,715)	(6,672)	3,037
Exchange Rate Effect on Cash from Continuing Operations	(6,558)	1,945	2,538
Change in Cash from Discontinued Operation	1	2,594	3,146
(Decrease) Increase in Cash and Cash Equivalents from Continuing Operations	(21,414)	21,919	(1,188)
Cash and Cash Equivalents at Beginning of Year	61,553	39,634	40,822
Cash and Cash Equivalents at End of Year	$ 40,139	$ 61,553	$ 39,634

See Note 1 for supplemental cash flow information.
The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statement of Comprehensive (Loss) Income and Shareholders' Investment

(In thousands, except par value	2008	2007	2006
Comprehensive (Loss) Income			
Net (Loss) Income	$ (22,558)	$ 22,668	$ 17,097
Other Comprehensive Items (Note 13):			
Foreign currency translation adjustment	(14,861)	10,859	7,909
Pension and other post-retirement liability adjustments, net (net of tax of $52 and $378 in 2008 and 2007, respectively)	(5,510)	(999)	–
Deferred loss on hedging instruments (net of tax of $200, $95 and $141 in 2008, 2007, and 2006, respectively)	(1,715)	(33)	(212)
Other Comprehensive Items	(22,086)	9,827	7,697
Comprehensive (Loss) Income	$ (44,644)	$ 32,495	$ 24,794
Shareholders' Investment			
Common Stock, $.01 Par Value:			
Balance at beginning and end of year	$ 146	$ 146	$ 146
Capital in Excess of Par Value:			
Balance at beginning of year	91,753	93,002	97,297
Activity under employees' and directors' stock plans	631	(4,195)	(6,700)
Tax benefit related to employees' and directors' stock plans	532	2,946	2,529
Adoption of SFAS 123R	–	–	(124)
Balance at end of year	92,916	91,753	93,002
Retained Earnings:			
Balance at beginning of year	175,106	153,147	136,050
Net (loss) income	(22,558)	22,668	17,097
Adoption of FIN 48	–	(709)	–
Balance at end of year	152,548	175,106	153,147
Treasury Stock, at Cost:			
Balance at beginning of year	(4,152)	(14,401)	(24,254)
Purchases of Company common stock	(48,454)	(5,185)	(7,181)
Activity under employees' and directors' stock plans	5,899	15,434	17,034
Balance at end of year	(46,707)	(4,152)	(14,401)
Deferred Compensation:			
Balance at beginning of year	–	–	(124)
Adoption of SFAS 123R	–	–	124
Balance at end of year	–	–	–
Accumulated Other Comprehensive Items (Note 13):			
Balance at beginning of year	15,898	6,071	(1,490)
Other comprehensive items	(22,086)	9,827	7,561
Balance at end of year	(6,188)	15,898	6,071
Shareholders' Investment	$192,715	$278,751	$237,965

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

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Kadant Inc. and its subsidiaries' (collectively, the Company) continuing operations include one operating segment, Pulp and Papermaking Systems (Papermaking Systems), and two separate product lines reported in Other Businesses, Fiber-based Products and Casting Products, through its sale in April 2007. Through its Papermaking Systems segment, the Company develops, manufactures, and markets a range of equipment and products for the global papermaking and paper recycling industries. The Company's principal products in this segment include custom-engineered stock-preparation systems and equipment for the preparation of wastepaper for conversion into recycled paper; fluid-handling systems used primarily in the dryer section of the papermaking process and during the production of corrugated boxboard, metals, plastics, rubber, textiles, and food; paper machine accessory equipment and related consumables important to the efficient operation of paper machines; and water-management systems essential for draining, purifying, and recycling process water. Through its Fiber-based Products line, the Company manufactures and sells granules derived from papermaking byproducts primarily for use as agricultural carriers and for home lawn and garden applications. The Company manufactured grey and ductile iron castings through its Casting Products business until its sale in April 2007.

On October 21, 2005, the Company's Kadant Composites LLC subsidiary (Composites LLC) sold its composites business, which is presented as a discontinued operation in the accompanying consolidated financial statements. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including warranty obligations related to products manufactured prior to the sale date. Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. At January 3, 2009, the accrued warranty costs for Composites LLC were $2,142,000, which represents the low end of the range of potential loss for products under warranty based on the level of claims received through the end of 2007. Composites LLC has calculated that the potential warranty cost ranges from $2,142,000 to approximately $13,100,000. See *Warranty Obligation for Discontinued Operation* below for further information. All future activity associated with this warranty reserve will continue to be classified in the results of the discontinued operation in the Company's consolidated financial statements. See Note 7 for information related to pending litigation associated with the composites business.

Company History and Former Relationship with Thermo Electron Corporation

The Company was incorporated in November 1991 to be the successor-in-interest to several papermaking equipment businesses of Thermo Electron Corporation (Thermo Electron). In November 1992, the Company completed an initial public offering of a portion of its common stock. On July 12, 2001, the Company changed its name to Kadant Inc. from Thermo Fibertek Inc. Thermo Electron disposed of its remaining equity interest in the Company by means of a dividend to Thermo Electron shareholders on August 8, 2001 (Spinoff Date). On May 14, 2003, the Company began trading on the New York Stock Exchange under the ticker symbol "KAI." Previously, the Company's common stock traded on the American Stock Exchange under the same symbol.

Principles of Consolidation

The accompanying consolidated financial statements of the Company include the accounts of its wholly and majority-owned subsidiaries. All material intercompany accounts and transactions have been eliminated.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Fiscal Year

The Company has adopted a fiscal year ending on the Saturday nearest to December 31. References to 2008, 2007, and 2006 are for the fiscal years ended January 3, 2009, December 29, 2007, and December 30, 2006, respectively. Prior to 2006, the Company's Kadant Lamort subsidiary, based in France, had a fiscal year ending on November 30 to allow sufficient time for the Company to consolidate the financial statements of that business. In 2006, the Kadant Lamort subsidiary changed its fiscal year end to conform to the Company's fiscal year end. This change resulted in the inclusion of an additional month of operating results for Kadant Lamort, which had an immaterial effect on the Company's consolidated income from continuing operations and net income in 2006.

Use of Estimates and Critical Accounting Policies

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period.

Critical accounting policies are defined as those that entail significant judgments and estimates, and could potentially result in materially different results under different assumptions and conditions. The Company believes that the most critical accounting policies upon which its financial position depends, and which involve the most complex or subjective decisions or assessments, concern revenue recognition and accounts receivable, warranty obligations for continuing operations and the discontinued operation, stock-based compensation, pension obligations, income taxes, accounts receivable, inventories, derivatives, and the valuation of intangible assets and goodwill. A discussion on the application of these and other accounting policies is included in Note 1.

Although the Company makes every effort to ensure the accuracy of the estimates and assumptions used in the preparation of its consolidated financial statements or in the application of accounting policies, if business conditions were different, or if the Company used different estimates and assumptions, it is possible that materially different amounts could be reported in the Company's consolidated financial statements.

Revenue Recognition and Accounts Receivable

The Company recognizes revenue under Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition." Revenue is generally recognized when products are delivered or services are performed. The Company includes in revenue amounts invoiced for shipping and handling with the corresponding costs reflected in cost of revenues. When the terms of the sale include customer acceptance provisions, and compliance with those provisions cannot be demonstrated until customer acceptance, revenues are recognized upon such acceptance.

Due to the significance of the Company's capital goods and spare parts businesses, most of the Company's revenue is recognized in accordance with the accounting policies in the preceding paragraph. However, when a sale arrangement involves multiple elements (e.g., installation), the Company considers the guidance in Emerging Issues Task Force (EITF) 00-21, "Revenue Arrangements with Multiple Deliverables." Such transactions are evaluated to determine whether the deliverables in the arrangement represent separate units of accounting. If equipment and installation do not meet the separation criteria under EITF 00-21, revenues for products sold that require installation for which the installation is essential to functionality, or is not deemed inconsequential or perfunctory, are recognized upon completion of installation. Revenues for products sold where installation is not essential to functionality, and is deemed inconsequential or perfunctory, are recognized upon shipment with estimated installation costs accrued.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

In addition, revenues and profits on certain long-term contracts are recognized using the percentage-of-completion method pursuant to Statement of Position No. 81-1, “Accounting for Performance of Construction-Type and Certain Production-Type Contracts.” Revenues recorded under the percentage-of-completion method were $58,077,000 in 2008, $103,489,000 in 2007, and $91,947,000 in 2006. The percentage of completion is determined by comparing the actual costs incurred to date to an estimate of total costs to be incurred on each contract. If a loss is indicated on any contract in process, a provision is made currently for the entire loss. The Company’s contracts generally provide for billing of customers upon the attainment of certain milestones specified in each contract. Revenues earned on contracts in process in excess of billings are classified as unbilled contract costs and fees, and amounts billed in excess of revenues earned are classified as billings in excess of contract costs and fees, which are included in other current liabilities in the accompanying balance sheet. There are no significant amounts included in the accompanying balance sheet that are not expected to be recovered from existing contracts at current contract values, or that are not expected to be collected within one year, including amounts that are billed but not paid under retainage provisions.

The Company exercises judgment in determining its allowance for bad debts, which is based on its historical collection experience, current trends, credit policies, specific customer collection issues, and accounts receivable aging categories. In determining this allowance, the Company looks at historical writeoffs of its receivables. The Company also looks at current trends in the credit quality of its customer base as well as changes in its credit policies. The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and each customer’s current creditworthiness. The Company continuously monitors collections and payments from its customers. In some instances, the Company utilizes letters of credit as a way to mitigate its credit exposure. In addition, the Company obtains letters of credit, principally issued by banks in China, related to certain contracts with its Chinese customers under which revenue is recognized using the percentage-of-completion method of accounting. While actual bad debts have historically been within its expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same rate of bad debts that it has had in the past, especially in light of current business conditions in the paper industry. A significant change in the liquidity or financial position of any of the Company’s customers could result in the uncollectibility of the related accounts receivable and could adversely affect its operating cash flows in that period.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Warranty Obligations for Continuing Operations

The Company provides for the estimated cost of product warranties at the time of sale based on the actual historical occurrence rates and repair costs. The Company typically negotiates the terms regarding warranty coverage and length of warranty depending on the products and applications. While the Company engages in extensive product quality programs and processes, the Company's warranty obligation is affected by product failure rates, repair costs, service delivery costs incurred in correcting a product failure, and supplier warranties on parts delivered to the Company. Should actual product failure rates, repair costs, service delivery costs, or supplier warranties on parts differ from the Company's estimates, revisions to the estimated warranty liability would be required. The changes in the carrying amount of accrued warranty costs included in other current liabilities in the accompanying consolidated balance sheet are as follows:

(In thousands)	2008	2007
Balance at Beginning of Year	$ 3,619	$ 3,164
Provision charged to income	4,233	3,516
Usage	(4,040)	(3,242)
Currency translation	(141)	181
Balance at End of Year	$ 3,671	$ 3,619

Warranty Obligations for Discontinued Operation

In 2005, Composites LLC sold its composites business and retained certain liabilities associated with the operation of the business prior to the sale, including the warranty obligations associated with products manufactured prior to the sale date. Activity associated with the warranty reserve is classified in the results of the discontinued operation in the Company's consolidated financial statements. Through the sale date, Composites LLC offered a standard limited warranty to the owner of its decking and roofing products, limited to repair or replacement of the defective product or a refund of the original purchase price.

Through the second quarter of 2006, Composites LLC recorded an estimate for warranty-related costs at the time of sale based on its actual historical return rates and repair costs, as well as other analytical tools for estimating future warranty claims. These estimates were revised for variances between actual and expected claims rates. Composites LLC's analysis of expected warranty claims rates included detailed assumptions associated with potential product returns, including the type of product sold, temperatures at the location of installation, density of boards, and other factors. Certain assumptions, such as the effect of weather conditions and high temperatures on the product installed, included inherent uncertainties that contributed to variances between actual and expected claims rates.

During the third quarter of 2006, Composites LLC concluded that the assumptions noted above were not accurately predicting the actual level of warranty claims, making it no longer possible to calculate a reasonable estimate of the future level of potential warranty claims. Accordingly, as no amount within the total range of loss represents a best estimate of the ultimate loss to be recorded, the Company is required under Statement of Financial Accounting Standards (SFAS) No. 5 (SFAS 5), "Accounting for Contingencies," to record the minimum amount of the potential range of loss for products under warranty. As of January 3, 2009, the accrued warranty costs associated with the composites business were $2,142,000, which represent the low end of the estimated range of warranty reserve required based on the level of claims received through the end of 2008. Composites LLC has calculated that the total potential warranty cost ranges from $2,142,000 to approximately $13,100,000. The high end of the range represents the estimated maximum level of warranty claims remaining

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

based on the total sales of the products under warranty. Composites LLC will continue to record adjustments to accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments entered against it in litigation, if any.

Income Taxes

In accordance with SFAS No. 109, "Accounting for Income Taxes," (SFAS 109) the Company recognizes deferred income taxes based on the expected future tax consequences of differences between the financial statement basis and the tax basis of assets and liabilities, calculated using enacted tax rates in effect for the year in which the differences are expected to reverse. A tax valuation allowance is established, as needed, to reduce net deferred tax assets to the amount expected to be realized. In the event it becomes more likely than not that some or all of the deferred tax asset allowances will not be needed, the valuation allowance will be adjusted.

The Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes—An Interpretation of FASB Statement No. 109," on December 31, 2006. It is the Company's policy to provide for uncertain tax positions and the related interest and penalties based upon management's assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities. At January 3, 2009, the Company believes that it has appropriately accounted for any unrecognized tax benefits. To the extent the Company prevails in matters for which a liability for an unrecognized tax benefit is established or is required to pay amounts in excess of the liability, its effective tax rate in a given financial statement period may be affected.

Prior to the spinoff from Thermo Electron, the Company and Thermo Electron were parties to a tax allocation agreement under which the Company and its subsidiaries, except its foreign operations, its Fiberprep subsidiary, and in 2000, its Kadant Composites Inc. subsidiary, were included in the consolidated federal and certain state income tax returns filed by Thermo Electron. The tax allocation agreement provided that, in years in which these entities had taxable income, the Company would pay to Thermo Electron amounts comparable to the taxes it would have paid if the Company had filed separate tax returns. The tax allocation agreement terminated as of the Spinoff Date, at which time the Company and Thermo Electron entered into a tax matters agreement. The tax matters agreement requires, among other things, that the Company file its own income tax returns for tax periods beginning immediately after the Spinoff Date. In addition, the tax matters agreement requires that the Company indemnify Thermo Electron, but not the shareholders of Thermo Electron, against liability for taxes resulting from (a) the conduct of the Company's business following the distribution or (b) the failure of the distribution to Thermo Electron shareholders of shares of the Company's common stock or of Viasys Healthcare Inc. (another Thermo Electron spinoff) common stock to continue to qualify as a tax-free spinoff under Section 355 of the Internal Revenue Code as a result of certain actions that the Company takes following the distribution. Thermo Electron has agreed to indemnify the Company against taxes resulting from the conduct of Thermo Electron's business prior to and following the distribution, or from the failure of the distribution of shares of the Company's common stock to Thermo Electron shareholders to continue to qualify as a tax-free spinoff other than as a result of some actions that the Company may take following the distribution. Although not anticipated, if any of the Company's post-distribution activities cause the distribution to become taxable, the Company could incur a liability to Thermo Electron and/or various taxing authorities, which could adversely affect the Company's results of operations, financial position, and cash flows.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Earnings per Share

Basic earnings per share has been computed by dividing net income by the weighted average number of shares outstanding during the year. Diluted earnings per share was computed assuming the effect of all potentially dilutive securities, including stock options and restricted stock awards, as well as their related tax effects.

Cash and Cash Equivalents

At year-end 2008 and 2007, the Company's cash equivalents included investments in money market funds and other marketable securities of its domestic and foreign subsidiaries, which had maturities of three months or less at the date of purchase. The carrying amounts of cash equivalents approximate their fair values due to the short-term nature of these instruments.

Supplemental Cash Flow Information

(In thousands)	2008	2007	2006
Cash Paid for Interest	$ 2,732	$ 3,182	$ 3,232
Cash Paid for Income Taxes	$ 4,340	$ 5,095	$ 2,250
Non-Cash Investing Activities (Note 2):			
Fair Value of Assets Acquired	$ –	$ –	$ 26,249
Cash Paid for Acquired Business	–	–	(20,520)
Liabilities Assumed of Acquired Business	$ –	$ –	$ 5,729
Non-Cash Financing Activities:			
Issuance of Restricted Stock	$ 488	$ 464	$ 478

Inventories

Inventories are stated at the lower of cost (on a first-in, first-out; or weighted average basis) or market value and include materials, labor, and manufacturing overhead. The Company periodically reviews its quantities of inventories on hand and compares these amounts to the expected usage of each particular product or product line. The Company records as a charge to cost of revenues any amounts required to reduce the carrying value of inventories to net realizable value. The components of inventories are as follows:

(In thousands)	2008	2007
Raw Materials and Supplies	$21,687	$23,587
Work in Process	16,230	9,855
Finished Goods (includes $2,452 and $2,405 at customer locations)	17,845	14,028
	$55,762	$47,470

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Property, Plant, and Equipment

Property, plant and equipment are stated at cost. The costs of additions and improvements are capitalized, while maintenance and repairs are charged to expense as incurred. The Company provides for depreciation and amortization primarily using the straight-line method over the estimated useful lives of the property as follows: buildings, 10 to 40 years; machinery and equipment, 2 to 10 years; and leasehold improvements, the shorter of the term of the lease or the life of the asset. Property, plant, and equipment consist of the following:

(In thousands)	2008	2007
Land	$ 4,629	$ 5,251
Buildings	36,495	37,672
Machinery, Equipment, and Leasehold Improvements	62,101	62,966
	103,225	105,889
Less: Accumulated Depreciation and Amortization	61,587	63,985
	$ 41,638	$ 41,904

Depreciation and amortization expense was $5,040,000, $4,871,000, and $4,960,000 in 2008, 2007, and 2006, respectively.

Intangible Assets

Intangible assets in the accompanying balance sheet include the costs of acquired intellectual property, tradename, patents, customer relationships, non-compete agreements and other specifically identifiable intangible assets. An intangible asset of $8,100,000 associated with the acquisition of the Johnson tradename as part of the Company’s acquisition of The Johnson Corporation in 2005 has an indefinite life and is not being amortized. The remaining intangible assets have been amortized using the straight-line method over periods ranging from 1 to 20 years with a weighted-average amortization period of 14 years. The intangible asset lives have been determined based on the anticipated period over which the Company will derive future cash flow benefits from the intangible assets. The Company has considered the effects of legal, regulatory, contractual, competitive, and other economic factors in determining these useful lives.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Acquired intangible assets are as follows:

(In thousands)	Gross	Currency Translation	Accumulated Amortization	Net
January 3, 2009				
Customer relationships	$16,308	$ 1,025	$ (4,293)	$13,040
Intellectual property	13,057	–	(6,291)	6,766
Tradename	8,100	–	–	8,100
Non-compete agreements	3,119	–	(3,119)	–
Distribution network	2,400	–	(518)	1,882
Licensing agreements	400	–	(73)	327
	$43,384	$ 1,025	$ (14,294)	$30,115
December 29, 2007				
Customer relationships	$16,308	$ 1,364	$ (3,013)	$14,659
Intellectual property	13,057	–	(5,252)	7,805
Tradename	8,100	–	–	8,100
Non-compete agreements	3,119	–	(3,114)	5
Distribution network	2,400	–	(372)	2,028
Licensing agreements	400	–	(53)	347
	$43,384	$ 1,364	$ (11,804)	$32,944

Amortization of acquired intangible assets was $2,490,000 in 2008, $2,492,000 in 2007 and $2,798,000 in 2006. The estimated future amortization expense of acquired intangible assets is $2,414,000 in 2009; $2,414,000 in 2010; $2,221,000 in 2011, $2,024,000 in 2012, $2,024,000 in 2013, and $10,918,000 in the aggregate thereafter.

Goodwill

Goodwill as of year-end 2008 and 2007 relates entirely to the Company's Papermaking Systems segment. The changes in the carrying amount of goodwill in 2008 and 2007 are as follows:

(In thousands)	2008	2007
Balance at Beginning of Year	$140,812	$137,078
Goodwill impairment	(40,333)	–
Decrease due to Kadant Johnson acquisition	(112)	(1,237)
Increase due to Kadant Jining acquisition	–	441
Currency translation adjustment	(5,337)	4,530
	$ 95,030	$140,812

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Impairment of Long-Lived Assets

The Company evaluates the recoverability of goodwill and intangible assets with indefinite useful lives annually in the fourth quarter, or more frequently if events or changes in circumstances, such as a decline in sales, earnings, or cash flows, or material adverse changes in the business climate, indicate that the carrying value of an asset might be impaired. During the fourth quarter of 2008, the Company experienced a significant decline in its stock price. As a result of the decline in the Company's stock price, its market capitalization fell significantly below the recorded value of its consolidated net assets. The reduced market capitalization reflected, in part, the current economic climate, which has led, and the Company believes will continue to lead, to weakness in demand for some of its products. The Company completed its impairment test in the fourth quarter of 2008 testing goodwill for impairment using the two-step method (as prescribed under SFAS No. 142, "Goodwill and Other Intangible Assets") on a "reporting unit" basis. The Company's reporting units are as follows: (1) stock-preparation (2) accessories and water management and (3) fluid handling. In step 1, goodwill is considered to be impaired when the net book value of a reporting unit exceeds its estimated fair value. The fair values of the reporting units were determined utilizing a discounted cash flow methodology and considered such assumptions as weighted average cost of capital, revenue growth, profitability, capital expenditures, and working capital requirements. These forecasts reflect an anticipated decline in stock-preparation equipment sales, especially in China, which the Company expects will occur over the next several years given the current economic environment and its impact on paper producers. As a result, the stock-preparation reporting unit failed step 1. In step 2, the Company calculated the implied fair value of goodwill for the stock-preparation reporting unit by deducting the estimated fair value of all tangible and intangible net assets (including unrecognized intangible assets) of the reporting unit from the fair value of the reporting unit as determined in step 1. The Company then compared the implied fair value of goodwill as determined in step 2 to the carrying value of goodwill. The impairment test indicated the carrying amounts of goodwill for the stock-preparation reporting unit within the Company's Papermaking Systems segment exceeded its implied fair value, and as a result, the Company recorded a $40,333,000 pre-tax ($26,712,000 after-tax) non-cash impairment charge to write down the goodwill associated with this reporting unit. The goodwill impairment test indicated that the estimated fair value of goodwill and indefinite-lived intangible assets associated with its other reporting units exceeded their carrying value and, as a result, no adjustment to goodwill was required for these reporting units. As part of the impairment test, the Company compares the sum of the estimated fair values of its reporting units with its fully diluted common stock market capitalization as a basis for concluding on the reasonableness of the estimated reporting units fair values.

The Company assesses its long-lived assets, other than goodwill and indefinite-lived intangible assets, for impairment whenever facts and circumstances indicate that the carrying amounts may not be fully recoverable. To analyze recoverability, the Company projects undiscounted net future cash flows over the remaining lives of such assets. If these projected cash flows were less than the carrying amounts, an impairment loss would be recognized, resulting in a write-down of the assets with a corresponding charge to earnings. The impairment loss would be measured based upon the difference between the carrying amounts and the fair values of the assets. In the fourth quarter of 2008, the Company experienced a significant decline in its stock price and its market capitalization, which the Company believes to be impairment indicators pursuant to SFAS No. 144, "Accounting for Impairment or Disposal of Long-Lived Assets". As a result, the Company performed an impairment test of its long-lived assets. No adjustment was required to the carrying value of its long-lived assets, excluding the goodwill impairment charge discussed above.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Foreign Currency Translation

All assets and liabilities of the Company's foreign subsidiaries are translated at year-end exchange rates, and revenues and expenses are translated at average exchange rates for each quarter in accordance with SFAS No. 52, "Foreign Currency Translation." Resulting translation adjustments are reflected in the "accumulated other comprehensive items" component of shareholders' investment (see Note 13). Foreign currency transaction gains and losses are included in the accompanying consolidated statement of operations and are not material for the three years presented.

Stock-Based Compensation

The Company recognizes compensation cost for all share-based payments to employees based on the grant date estimate of fair value for those awards. The Company uses the Black-Scholes option-pricing model to determine fair value for option grants and the grant date trading price of the Company's common stock to determine the fair value for restricted stock awards. Compensation expense is recognized ratably over the vesting period of the award.

Derivatives

The Company uses derivative instruments primarily to reduce its exposure to changes in currency exchange rates and interest rates. When the Company enters into a derivative contract, the Company makes a determination as to whether the transaction is deemed to be a hedge for accounting purposes. For contracts deemed to be a hedge, the Company formally documents the relationship between the derivative instrument and the risk being hedged. In this documentation, the Company specifically identifies the asset, liability, forecasted transaction, cash flow, or net investment that has been designated as the hedged item, and evaluates whether the derivative instrument is expected to reduce the risks associated with the hedged item. To the extent these criteria are not met, the Company does not use hedge accounting for the derivative.

SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133), as amended, requires that all derivatives be recognized on the balance sheet at fair value. For derivatives designated as cash flow hedges, the related gains or losses on these contracts are deferred as a component of accumulated other comprehensive items. These deferred gains and losses are recognized in the period in which the underlying anticipated transaction occurs. For derivatives designated as fair value hedges, the unrealized gains and losses resulting from the impact of currency exchange rate movements are recognized in earnings in the period in which the exchange rates change and offset the currency gains and losses on the underlying exposures being hedged. The Company performs an evaluation of the effectiveness of the hedge both at inception and on an ongoing basis. The ineffective portion of a hedge, if any, and changes in the fair value of a derivative not deemed to be a hedge, are recorded in the consolidated statement of operations.

The Company entered into interest rate swap agreements in 2008 and 2006 to hedge its exposure to variable rate debt and has designated these agreements as cash flow hedges. The fair values of the interest rate swap agreements are included in other assets for unrecognized gains and in other long-term liabilities for unrecognized losses with an offset in accumulated other comprehensive items (net of tax). The Company has structured these interest rate swap agreements to be 100% effective and as a result, there is no current impact to earnings resulting from hedge ineffectiveness.

The Company uses forward currency-exchange contracts primarily to hedge certain operational ("cash flow" hedges) and balance sheet ("fair value" hedges) exposures resulting from fluctuations in currency exchange rates. Such exposures primarily result from portions of the Company's operations and assets that are denominated in

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

currencies other than the functional currencies of the businesses conducting the operations or holding the assets. As part of the Company's overall strategy to manage the level of exposure to the risk of currency-exchange fluctuations, some of its subsidiaries hedge a portion of their currency exposures anticipated over the ensuing 12-month period, using forward currency-exchange contracts that have maturities of 12 months or less. The Company does not hold or engage in transactions involving derivative instruments for purposes other than risk management.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141(R) "Business Combinations" (SFAS 141(R)), which replaces SFAS No. 141. SFAS 141(R) requires the acquiring entity in a business combination to recognize the assets acquired and the liabilities assumed in the transaction, establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed, and requires the acquirer to disclose certain information to enable users to evaluate and understand the nature and financial effects of the business combination. SFAS 141(R) also requires that cash outflows, such as transaction costs and post-acquisition restructuring costs, be charged to expense instead of capitalized as a cost of the acquisition. Contingent purchase price will be recorded at its initial fair value and then re-measured as time passes through adjustments to net income. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. The adoption of SFAS 141(R) will have an impact on accounting for business combinations completed subsequent to its adoption and for certain transactions prior to adoption. As of January 3, 2009, the Company had a tax valuation allowance of $1,012,000 relating to the Kadant Johnson Inc. acquisition, a liability for unrecognized tax benefits of $517,000, and accrued interest and penalties of $843,000, all of which would have affected goodwill if recognized prior to the end of fiscal 2008, but will now affect the Company's annual effective tax rate if recognized.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements—an Amendment of Accounting Research Bulletin No. 51" (SFAS 160), which establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest and the valuation of retained non-controlling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners. SFAS 160 is effective for fiscal years beginning after December 15, 2008. The Company does not believe that the adoption of this statement will have a material affect on its consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" (SFAS 161). SFAS 161 requires disclosures of how and why an entity uses derivative instruments; how derivative instruments and related hedged items are accounted for; and how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. SFAS 161 is effective for fiscal years beginning after November 15, 2008. The adoption of SFAS 161 will change the Company's disclosures for derivative instruments and hedging activities beginning in the first quarter of 2009.

In April 2008, the FASB issued FASB Staff Position (FSP) FAS 142-3, "Determination of the Useful Life of Intangible Assets" (FSP FAS 142-3). FSP FAS 142-3 amends the factors that should be considered in developing the 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 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. The Company does not believe that the adoption of FSP FAS 142-3 will have a material affect on its consolidated financial statements.

Notes to Consolidated Financial Statements

1. Nature of Operations and Summary of Significant Accounting Policies (continued)

In December 2008, the FASB issued FSP No. 132(R)-1, "Employers' Disclosures about Postretirement Benefit Plan Assets" (FSP 132(R)-1). FSP 132(R)-1 requires additional disclosures about an employer's plan assets of defined benefit pension or other postretirement plans. This rule expands current disclosures of defined benefit pension and postretirement plan assets to include information regarding the fair value measurements of plan assets similar to the Company's current SFAS No. 157, "Fair Value Measurements", disclosures. FSP 132(R)-1 is effective for fiscal years ending after December 15, 2009. The Company is currently evaluating the potential impact of the adoption of FSP 132(R)-1 on its financial statement disclosures.

Reclassifications

Certain reclassifications have been made to the prior years' presentations to conform to the 2008 presentation.

2. Acquisition and Disposition

Acquisition

On June 2, 2006, the Company's subsidiary, Kadant Light Machinery (Jining) Co., Ltd. (Kadant Jining), assumed responsibility for the operation of Jining Huayi Light Industry Machinery Co., Ltd. (Huayi), and, by September 30, 2006, acquired substantially all of the assets of Huayi (Kadant Jining acquisition) including cash, inventory, machinery, equipment, and buildings for $21,153,000, net of assumed liabilities of $2,253,000 primarily related to acquired customer deposits. Of the total consideration, $17,331,000 was paid in cash, including $1,032,000 for acquisition-related costs. Of the remaining purchase obligation of $3,822,000, $3,593,000 was paid as of January 3, 2009 and the remainder will be paid if certain indemnification obligations are satisfied. Huayi was a supplier of stock-preparation equipment in China. The Company believes that the acquisition of this business will allow the Company to deliver its stock-preparation systems and aftermarket products to customers in China more efficiently, supply parts and components to North America and Europe, and extend the Company's customer base to include more small-to-midsize mills in China.

This acquisition was accounted for under the purchase method of accounting and the operating results for Kadant Jining have been included in the accompanying consolidated financial statements from the acquisition date of June 2, 2006. The following table summarizes the purchase method of accounting for this acquisition (in thousands):

Allocation of Purchase Price:	
Cash and Cash Equivalents	$ 2,180
Inventory	2,312
Other Current Assets	415
Property, Plant, and Equipment	8,928
Other Assets	3,254
Intangible Assets	608
Goodwill	5,709
Total Assets Acquired	23,406
Current Liabilities Assumed	2,253
Net Assets Acquired	$ 21,153
Consideration:	
Cash	$ 11,227
Debt	5,072
Short- and Long-Term Obligations	3,822
Acquisition Costs	1,032
Total Consideration	$ 21,153

The allocation of the purchase price was based on the fair value of the assets acquired. Intangible assets of $608,000 relate to customer relationships with a five year useful life. The excess of the purchase price over the tangible and identifiable intangible assets was recorded as goodwill and amounted to approximately $5,709,000, which is fully deductible for tax purposes. The Company recorded an impairment charge at the end of 2008 to write down a portion of this goodwill. See *Impairment of Long-Lived Assets* in Note 1 for further information.

Pro forma disclosure of the results of operations as if the Kadant Jining acquisition had occurred at the beginning of 2006 is not required, as the acquisition did not meet the definition of a material business combination outlined in SFAS No. 141, "Business Combinations."

2. Acquisition and Disposition (continued)

The Company's acquisitions have historically been made at prices above the fair value of the acquired assets, resulting in goodwill, due to the expectation of synergies of combining the businesses. The synergies expected as a result of the acquisitions include the use of the Company's existing infrastructure such as its sales force, distribution channels and customer relations to expand sales of the acquiree's products; use of the acquiree's infrastructure to cost effectively expand sales of the Company's products; and elimination of duplicative functions. In accordance with current accounting standards, goodwill will not be amortized and will be tested for impairment annually (in the fourth quarter of the Company's fiscal year) as required by SFAS No. 142, "Goodwill and Other Intangible Assets."

Disposition

On April 30, 2007, the Company's Kadant Johnson Holdings Inc. (formerly Specialty Castings Inc.) subsidiary sold substantially all the assets of its Casting Products business for $390,000, consisting of $250,000 received in cash at closing and a $140,000 note receivable, which was collected in 2008. The Company recorded a pre-tax loss of $388,000 ($233,000 after-tax, or $.02 per diluted share) on the sale in 2007.

3. Employee Benefit Plans

Stock-Based Compensation Plans

The Company maintains stock-based compensation plans primarily for its key employees and directors, although the plans permit awards to others expected to make significant contributions to the future of the Company. The plans authorize the compensation committee of the Company's board of directors (the board committee) to award a variety of stock and stock-based incentives, such as restricted stock, nonqualified and incentive stock options, stock bonus shares, or performance-based shares. The award recipients and the terms of awards, including price, granted under these plans are determined by the board committee. Upon a change-of-control, as defined in the plans, all options or other awards become fully vested and all restrictions lapse. The Company had 828,651 shares available for grant under stock-based compensation plans at January 3, 2009.

In accordance with SFAS No. 123R, "Share-Based Payment" (SFAS 123R), the Company recognizes compensation cost for all share-based payments to employees based on the grant date estimate of fair value for those awards. The Company uses the Black-Scholes option-pricing model to determine fair value for option grants and the grant date trading price of the Company's common stock to determine the fair value for restricted stock awards. Compensation expense is recognized ratably over the vesting period of the award. The total share-based compensation expense was $2,945,000, $1,796,000, and $926,000 in 2008, 2007, and 2006, respectively, and is included in selling, general, and administrative expenses in the accompanying consolidated statement of operations.

Restricted Shares and Restricted Stock Unit Awards

On March 3, 2008, the Company granted an aggregate of 20,000 restricted stock units (RSUs) to its outside directors with an aggregate fair value of $488,000, which vested at a rate of 5,000 shares per quarter on the last day of each quarter in 2008. The March 3, 2008 awards also included an aggregate of 40,000 RSUs with an aggregate fair value of $975,000, which will only vest and compensation expense will only be recognized upon a change in control as defined in the Company's 2006 equity incentive plan. The 40,000 RSUs will be forfeited if a change in control does not occur by the end of the first quarter of 2009.

3. Employee Benefit Plans (continued)

In February 2007, the Company granted an aggregate of 40,000 restricted shares with an aggregate fair value of $928,000 to its outside directors, which only would have vested if a change in control had occurred prior to the end of the first quarter of 2008. These restricted shares were forfeited at the end of the first quarter of 2008 with no compensation expense recognized.

Performance-Based Restricted Stock Units

On March 3, 2008, the Company granted to certain officers of the Company performance-based RSUs, which represent, in aggregate, the right to receive 93,000 shares (the target RSU amount), subject to adjustment, with a grant date fair value of $25.07 per share. The RSUs will cliff vest in their entirety on the last day of the Company's 2010 fiscal year, provided that the officer remains employed by the Company through the vesting date. The target RSU amount was subject to adjustment based on the achievement of specified EBITDA targets generated from continuing operations for the 2008 fiscal year, which were met, and resulted in an adjusted RSU amount of 47,430 shares deliverable upon vesting.

On May 24, 2007, the Company granted to certain of its officers performance-based RSUs, which represented, in aggregate, the right to receive 104,000 shares (the target RSU amount), subject to adjustment, with a grant date fair value of $28.21 per share. The RSUs will cliff vest in their entirety on the last day of the Company's 2009 fiscal year, provided that the officer remains employed by the Company through the vesting date. The target RSU amount was subject to adjustment based on the achievement of specified EBITDA targets generated from continuing operations for the nine-month period ended December 29, 2007, which were exceeded, and resulted in an adjusted RSU amount of 134,160 shares deliverable upon vesting.

The performance-based RSU agreements provide for forfeiture in certain events, such as voluntary or involuntary termination of employment, and for acceleration of vesting in certain events, such as death, disability or a change in control of the Company. If the officer dies or is disabled prior to the vesting date, then a ratable portion of the RSUs will vest. If a change in control occurs prior to the end of the performance period, the officer will receive the target RSU amount; otherwise, the officer will receive the number of deliverable RSUs based on the achievement of the performance goal, as stated in the RSU agreements.

Each performance-based RSU represents the right to receive one share of the Company's common stock upon vesting. The Company is recognizing compensation expense associated with performance-based RSUs ratably over the vesting period based on the grant date fair value. Compensation expense of $1,817,000 and $869,000 was recognized in 2008 and 2007, respectively, associated with these performance-based RSUs. Unrecognized compensation expense related to the unvested performance-based RSUs totaled approximately $2,281,000 at January 3, 2009 and will be recognized over a weighted average period of 1.4 years.

Time-Based Restricted Stock Units

The Company granted 61,550 time-based RSUs on May 24, 2007 with a grant date fair value of $28.21 per share, 12,000 time-based RSUs on March 3, 2008 with a grant date fair value of $25.07 per share, and 600 time-based RSUs on September 15, 2008 with a grant date fair value of $24.00 per share, to certain employees of the Company. Each time-based RSU represents the right to receive one share of the Company's common stock upon vesting. The time-based RSUs will cliff vest in their entirety provided the recipients remain employed with the Company through the vesting date. The time-based RSUs (net of forfeitures) will vest as follows: 600 on December 31, 2009, 59,950 on May 24, 2011, and 12,000 on March 3, 2012. The time-based RSU agreement provides for forfeiture in certain events, such as voluntary or involuntary termination of employment, and for acceleration of vesting in certain events, such as death, disability, or a change in control of the Company. The Company is recognizing compensation expense associated with these time-based RSUs ratably over the vesting

Notes to Consolidated Financial Statements

3. Employee Benefit Plans (continued)

period based on the grant date fair value. Compensation expense of $496,000 and $260,000, respectively, was recognized in 2008 and 2007 associated with these time-based RSUs. Unrecognized compensation expense related to the time-based RSUs totaled approximately $1,257,000 as of January 3, 2009 and will be recognized over a weighted average period of 2.6 years.

A summary of the status of the Company's unvested restricted share/unit awards for year-end 2008 is as follows:

Unvested Restricted Share/Unit Awards	Shares/Units (In thousands)	Weighted Average Grant-Date Fair Value
Unvested at December 29, 2007	236	$ 27.36
Granted	120	$ 24.72
Vested	(20)	$ 24.38
Forfeited / Expired	(42)	$ 23.39
Unvested at January 3, 2009	294	$ 27.05

Stock Options

Outstanding options granted prior to 2001 are nonqualified options that are exercisable immediately, but are subject to provisions similar to vesting that restrict transfer and afford the Company the right to repurchase the shares at the exercise price upon certain events. The restrictions and repurchase rights for these options generally lapse over five to ten years and the terms of the options may range from five to twelve years. Options granted in 2001 and after have been nonqualified options that vest over three years and are not exercisable until vested. To date, all options have been granted at an exercise price equal to the fair market value of the Company's common stock on the date of grant. The Company generally issues its common stock out of treasury stock to satisfy option exercises. The Company did not grant stock options in 2008, 2007, or 2006.

A summary of the Company's stock option activity for 2008 is as follows:

(In thousands, except per share amounts)	Number of Shares	Weighted Average Exercise Price(a)	Weighted Average Remaining Contractual Life
Options Outstanding, Beginning of Year	293	$ 22.59	
Granted	–	–	
Exercised	(196)	14.79	
Expired	(13)	17.55	
Options Outstanding and Exercisable, End of Year	84	$ 41.46	1.2 years

(a) Market price per share on January 3, 2009 was $13.58.

Notes to Consolidated Financial Statements

3. Employee Benefit Plans (continued)

A summary of the Company's stock option exercises in 2008, 2007, and 2006 are as follows:

(In thousands)	2008	2007	2006
Total intrinsic value of options exercised	$1,534	$8,508	$7,492
Cash received from options exercised	2,894	9,225	9,380
Income tax benefits from options exercised	544	2,893	2,529

Employee Stock Purchase Plan

Substantially all of the Company's full-time U.S. employees are eligible to participate in its employee stock purchase plan. Under the plan, shares of the Company's common stock may be purchased at a 15% discount from the fair market value at the beginning or end of the purchase period, whichever is lower. Shares purchased under the plan are subject to a one-year resale restriction and are purchased through payroll deductions of up to 10% of each participating employee's gross wages. For the 2008, 2007, and 2006 plan years, the Company issued 24,816 shares, 19,639 shares, and 22,007 shares, respectively, of its common stock under this plan.

Profit-Sharing, 401(k) Savings and Other Defined Contribution Plans

Several of the Company's U.S. subsidiaries participate in the Company's 401(k) retirement savings plan. Contributions to the plan are made by both the employee and the Company. Company contributions are based upon the level of employee contributions.

Through October 2, 2006, one of the Company's U.S. subsidiaries had a 401(k) retirement savings plan with a profit-sharing feature under which the Company annually contributed approximately 10% of the subsidiary's pre-tax income before profit-sharing expense. Effective October 2, 2006, the Company eliminated the profit-sharing feature and replaced it with Company contributions based on the level of employee contributions. All contributions related to this plan are immediately vested.

Through June 30, 2006, another of the Company's U.S. subsidiaries had a 401(k) retirement savings plan with a profit-sharing feature that required a minimum annual Company contribution of 3% of eligible employee compensation and allowed for an additional contribution of up to 12% of eligible compensation at the discretion of the Company. Effective July 1, 2006, the total Company contribution was reduced to 6% of eligible compensation. Effective January 1, 2007, this plan was restated to eliminate the profit-sharing feature and to base Company contributions on the level of employee contributions instead of eligible compensation. All contributions related to this plan are immediately vested.

Certain of the Company's subsidiaries offer other retirement plans, the majority of which are defined contribution plans. Company contributions to these plans are based on formulas determined by the Company.

For these plans, the Company contributed and charged to expense approximately $3,413,000, $3,342,000, and $3,446,000 in 2008, 2007, and 2006, respectively.

3. Employee Benefit Plans (continued)

Defined Benefit Pension Plan and Post-Retirement Welfare Benefits Plans

The Company’s Kadant Web Systems subsidiary has a noncontributory defined benefit retirement plan. Benefits under the plan are based on years of service and employee compensation. Funds are contributed to a trustee as necessary to provide for current service and for any unfunded projected benefit obligation over a reasonable period. Effective December 31, 2005, this plan was closed to new participants. Effective January 1, 2007, the provision limiting lump sum distributions upon termination of employment to $10,000 was removed. This same subsidiary also has a post-retirement welfare benefits plan (included in the table below in “Other Benefits”). No future retirees are eligible for this post-retirement welfare benefits plan, and the plans include limits on the subsidiary’s contributions.

The Company’s Kadant Lamort subsidiary sponsors a defined benefit pension plan (included in the table below in “Other Benefits”). Benefits under this plan are based on years of service and projected employee compensation.

The Company’s Kadant Johnson subsidiary also offers a post-retirement welfare benefits plan (included in the table below in “Other Benefits”) to its U.S. employees upon attainment of eligible retirement age. This post-retirement benefit plan was amended to reduce the annual subsidy provided under the plan effective January 1, 2007. In addition, this plan will be closed to employees who will not meet its retirement eligibility requirements on January 1, 2012.

On December 30, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158 (SFAS 158), “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans—An Amendment of FASB Statements No. 87, 88, 106, and 132(R).” SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income.

In accordance with SFAS 158, the Company recognized the funded status (i.e., the difference between the fair value of the plan assets and the projected benefit obligations) of its pension and other post-retirement plans in the December 30, 2006 consolidated balance sheet, with a corresponding adjustment to accumulated other comprehensive income, net of tax. The adjustment to accumulated other comprehensive income at adoption represents the net unrecognized actuarial gains (losses) and unrecognized prior service costs (income), all of which were previously netted against the plan’s funded status on the Company’s consolidated balance sheet pursuant to the provisions of SFAS No. 87, “Employers’ Accounting for Pensions” (SFAS 87). These amounts will be subsequently recognized as net periodic pension cost pursuant to the Company’s historical accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic pension cost in the same periods will be recognized as a component of accumulated other comprehensive items. The prior service income and actuarial loss included in accumulated other comprehensive items and expected to be recognized in net periodic pension cost in 2009 is $678,000 and $425,000, respectively.

Notes to Consolidated Financial Statements

3. Employee Benefit Plans (continued)

The following table summarizes the change in the benefit obligation; the change in plan assets; the funded status; and the amounts recognized in the balance sheets for the Company's pension benefits and other benefits plans. The measurement date for all items set forth below is the last day of the fiscal year presented.

	Pension Benefits		Other Benefits	
(In thousands)	2008	2007	2008	2007
Change in Benefit Obligation:				
Benefit obligation at beginning of year	$21,190	$20,072	$ 4,601	$ 4,760
Service cost	806	819	83	104
Interest cost	1,198	1,119	248	236
Actuarial (gain) loss	(201)	150	(206)	(362)
Benefits paid	(1,291)	(970)	(406)	(325)
Effect of currency translation	–	–	(73)	188
Benefit obligation at end of year	$21,702	$21,190	$ 4,247	$ 4,601
Change in Plan Assets:				
Fair value of plan assets at beginning of year	$18,219	$18,297	$ –	$ –
Actual return on plan assets	(4,248)	692	–	–
Employer contribution	1,600	200	406	326
Benefits paid	(1,291)	(970)	(406)	(326)
Fair value of plan assets at end of year	$14,280	$18,219	$ –	$ –
Unfunded status	$ (7,422)	$ (2,971)	$(4,247)	$(4,601)
Accumulated benefit obligation as of year-end	$18,083	$17,660	$ 1,452	$ 1,506
Information Related to Plans with Accumulated Benefit Obligations in Excess of Plan Assets:				
Projected benefit obligation	$21,702	$ –	$ 1,840	$ 1,913
Accumulated benefit obligation	$18,083	$ –	$ 1,452	$ 1,506
Fair value of plan assets	$14,280	$ –	$ –	$ –
Amounts Recognized in the Balance Sheet Consist of:				
Current liability	$ (2,556)	$ –	$ –	$ –
Non-current liability	(4,866)	(2,971)	(4,247)	(4,601)
Total amount recognized	$ (7,422)	$ (2,971)	$(4,247)	$(4,601)
Amounts Recognized in Accumulated Other Comprehensive Items Before Tax Consist of:				
Unrecognized net actuarial (loss) gain	$ (8,165)	$ (2,711)	$ 321	$ 127
Unrecognized prior service (cost) income	(494)	(549)	907	1,702
Total	$ (8,659)	$ (3,260)	$ 1,228	$ 1,829
Changes in Amounts Recognized in Accumulated Other Comprehensive Items Before Tax:				
Current year unrecognized net actuarial (loss) gain	$ (5,511)	$ (901)	$ 194	$ 372
Amortization of unrecognized prior service cost (income)	55	55	(795)	(794)
Amortization of unrecognized net actuarial loss	57	36	–	28
Total	$ (5,399)	$ (810)	$ (601)	$ (394)

Notes to Consolidated Financial Statements

3. Employee Benefit Plans (continued)

The weighted-average assumptions used to determine the benefit obligation as of year-end were as follows:

	Pension Benefits		Other Benefits	
	2008	2007	2008	2007
Discount rate	6.25%	6.00%	6.03%	5.79%
Rate of compensation increase	4.00%	4.00%	2.00%	2.00%

(In thousands)	Pension Benefits 2008	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2008	Other Benefits 2007	Other Benefits 2006
Components of Net Periodic Benefit Cost (Income):						
Service cost	$ 806	$ 819	$ 752	$ 83	$ 104	$ 190
Interest cost	1,198	1,119	1,048	248	236	323
Expected return on plan assets	(1,464)	(1,442)	(1,414)	–	–	–
Recognized net actuarial loss	57	36	60	–	28	33
Amortization of prior service cost (income)	55	55	47	(795)	(794)	(334)
Net periodic benefit cost (income)	$ 652	$ 587	$ 493	$ (464)	$ (426)	$ 212

The weighted-average assumptions used to determine net periodic benefit cost (income) were as follows:

	Pension Benefits 2008	Pension Benefits 2007	Pension Benefits 2006	Other Benefits 2008	Other Benefits 2007	Other Benefits 2006
Discount rate	6.00%	5.75%	5.75%	5.89%	5.45%	4.48%
Expected long-term return on plan assets	8.50%	8.50%	8.50%	–	–	–
Rate of compensation increase	4.00%	4.00%	4.00%	2.00%	2.00%	2.00%

In developing the overall expected long-term return on plan assets assumption, a building block approach was used in which rates of return in excess of inflation were considered separately for equity securities, debt securities, and other assets. The excess returns were weighted by the representative target allocation and added along with an appropriate rate of inflation to develop the overall expected long-term return on plan assets assumption. The Company believes this determination is consistent with SFAS 87.

Assumed weighted-average healthcare cost trend rates as of year-end were as follows:

	2008	2007
Healthcare cost trend rate assumed for next year	5.89%	7.00%
Ultimate healthcare cost trend rate	5.11%	5.11%
Year that the assumed rate reaches ultimate rate	2011	2011

Assumed healthcare cost trend rates can have a significant effect on the amounts reported for healthcare benefits. A one-percentage point change in assumed healthcare cost trend rates would have the following effects:

(In thousands)	1 Percentage Point Increase	1 Percentage Point Decrease
Effect on total of service and interest cost components—(expense) income	$ (12)	$ 10
Effect on post-retirement benefit obligation—(increase) decrease	$ (139)	$ 123

Notes to Consolidated Financial Statements

3. Employee Benefit Plans (continued)

Plan Assets

For the Kadant Web Systems noncontributory defined benefit retirement plan, the weighted-average asset allocation at January 3, 2009 and December 29, 2007, by asset category, is as follows:

Asset Category	2008	2007
Equity securities	41%	46%
Debt securities	50%	44%
Other	9%	10%
Total	100%	100%

Kadant Web Systems has developed an investment policy for the noncontributory defined benefit retirement plan. The investment strategy is to emphasize total return, that is, the aggregate return from capital appreciation and dividend and interest income. The primary objective of the investment management for the plan's assets is the emphasis on consistent growth, specifically, growth in a manner that protects the plan's assets from excessive volatility in market value from year to year. The investment policy takes into consideration the benefit obligations, including timing of distributions.

The primary objective for the plan is to provide long-term capital appreciation through investment in equity and debt securities. The following target asset allocation has been established for the plan:

Asset Category	Minimum	Neutral	Maximum
Equity securities	40%	45%	60%
Debt securities	30%	45%	50%
Other	5%	10%	15%
Total		100%	

All equity securities must be drawn from recognized securities exchanges. Debt securities must be weighted to reflect a portfolio average maturity of not more than ten years, with average benchmark duration of five years. The credit quality must equal or exceed high investment grade quality ("BAA" or better).

Cash Flows

Contributions

Four quarterly cash contributions of $1,200,000 each are expected for the Kadant Web Systems noncontributory defined benefit retirement plan in 2009. For the remaining pension and post-retirement welfare benefits plans, no cash contributions other than to fund current benefit payments are expected in 2009.

3. Employee Benefit Plans (continued)

Estimated Future Benefit Payments

The following benefit payments, which reflect future service as appropriate, are expected to be paid. The benefit payments are based on the same assumptions used to measure the Company's benefit obligation at year-end 2008.

(In thousands)	Pension Benefits	Other Benefits
2009	$2,556	$ 275
2010	1,745	364
2011	971	308
2012	1,831	328
2013	1,241	317
2014-2018	8,657	2,372

Information and Assumptions for the Post-Retirement Welfare Benefits Plan

Kadant Web Systems Post-Retirement Welfare Benefits Plan

All eligible retirees are currently participating in the Kadant Web Systems post-retirement welfare benefits plan, with no future retirees eligible to participate. Effective September 1, 2003, Kadant Web Systems capped its monthly contribution to the plan at $358 per participant. For the majority of the retirees in the plan, no healthcare cost trend rate is assumed, as the Company cap applies. For the remainder, the healthcare cost trend rate is assumed to be 7% in 2008, decreasing to an ultimate rate of 0% in 2012.

Kadant Johnson Post-Retirement Welfare Benefits Plan

All eligible retirees are currently participating in the Kadant Johnson post-retirement welfare benefits plan. Kadant Johnson pays 75% of all plan costs for retirees with a retirement date prior to January 1, 2005, and 50% of all plan costs for retirees with a retirement date after January 1, 2005, with no limits on its contributions up to annual employee and plan stop loss limitations. On August 17, 2006, this post-retirement benefit plan was amended to reduce the annual subsidy provided under the plan effective January 1, 2007. In addition, this plan will be closed to employees who will not meet its retirement eligibility requirements on January 1, 2012. The medical healthcare cost trend rate is assumed to be 6% in 2008, decreasing to an ultimate rate of 5% in 2011.

On December 8, 2003, Medicare reform legislation was enacted, providing a Medicare prescription drug benefit beginning in 2006 and federal subsidies to employers who provide drug coverage to retirees. Kadant Johnson applied for the federal subsidy during 2005 and 2006. The effect of the anticipated subsidy was recognized as of December 31, 2005. Given the plan changes made during 2006, the Company anticipates that it will not be eligible for the subsidy after 2011.

The following subsidy payments are expected to be received:

(In thousands)	Expected Part D Subsidy
2009	$ 35
2010	33
2011	33

Notes to Consolidated Financial Statements

4. Preferred and Common Stock

Preferred Stock

The Company's Certificate of Incorporation authorizes up to 5,000,000 shares of preferred stock, $.01 par value per share, for issuance by the Company's board of directors without further shareholder approval. The board of directors has also designated 15,000 shares of such preferred stock as Series A junior participating preferred stock for issuance under the Company's Shareholder Rights Plan (see below). No such preferred stock has been issued by the Company.

Common Stock

The Company has a Shareholder Rights Plan under which one right was distributed at the close of business on August 6, 2001 for each share of the Company's common stock outstanding at that time. The rights plan is designed to provide shareholders with fair and equal treatment in the event of an unsolicited attempt to acquire the Company. The rights were attached to the Company's outstanding common stock at the time of distribution and are not separately transferable or exercisable. The rights will become exercisable if a person acquires 15 percent or more of the Company's common stock, or a tender or exchange offer is commenced for 15 percent or more of the Company's common stock, unless, in either case, the transaction was approved by the Company's board of directors. If the rights become exercisable, each right will initially entitle the Company's shareholders to purchase .0001 of a share of the Company's Series A junior participating preferred stock, $.01 par value, at an exercise price of $75. In addition, except with respect to transactions approved by the Company's board of directors, if the Company is involved in a merger or other transaction with another company in which it is not the surviving corporation, or the Company sells or transfers 50 percent or more of its assets or earning power to another company, each right (other than rights owned by the acquirer) will entitle its holder to purchase $75 worth of the common stock of the acquirer at half the market value at that time. The Company is entitled to redeem the rights at $.001 per right at any time prior to the tenth business day (or later, if so determined by the board of directors) after the acquisition of 15 percent or more of the Company's common stock. Unless the rights are redeemed or exchanged earlier, they will expire on July 16, 2011.

At January 3, 2009, the Company had reserved 1,451,604 unissued shares of its common stock for possible issuance under its stock-based compensation plans.

5. Income Taxes

The components of (loss) income from continuing operations before provision for income taxes and minority interest expense are as follows:

(In thousands)	2008	2007	2006
Domestic	$(32,079)	$16,289	$14,813
Foreign	18,269	19,233	12,422
	$(13,810)	$35,522	$27,235

Notes to Consolidated Financial Statements

5. Income Taxes (continued)

The components of the provision for income taxes from continuing operations are as follows:

(In thousands)	2008	2007	2006
Current Provision:			
Federal	$ 241	$1,039	$ 146
Foreign	3,855	3,261	3,340
State	319	554	137
	4,415	4,854	3,623
Deferred Provision:			
Federal	4,373	5,092	5,101
Foreign	(8)	81	(296)
State	(314)	(243)	260
	4,051	4,930	5,065
	$8,466	$9,784	$8,688

The provision for income taxes included in the accompanying statement of operations is as follows:

(In thousands)	2008	2007	2006
Continuing Operations	$8,466	$ 9,784	$8,688
Discontinued Operation	(65)	(1,508)	(702)
	$8,401	$ 8,276	$7,986

The Company generally receives a tax deduction upon the exercise of nonqualified stock options by employees equal to the difference between the market price and the exercise price of the Company's common stock on the date of exercise. The current provision for income taxes does not reflect $544,000, $2,893,000, and $2,529,000 of such benefits from the exercise of stock options that have been allocated to capital in excess of par value in 2008, 2007, and 2006, respectively. In addition, in 2008 and 2007, there is an additional tax provision of $12,000 and tax benefit of $53,000, respectively, associated with restricted stock awards.

The provision for income taxes from continuing operations in the accompanying statement of operations differs from the provision calculated by applying the statutory federal income tax rate of 35% to (loss) income from continuing operations before provision for income taxes and minority interest expense due to the following:

(In thousands)	2008	2007	2006
(Benefit) Provision for Income Taxes at Statutory Rate	$ (4,833)	$12,433	$ 9,532
Increases (Decreases) Resulting From:			
State income taxes, net of federal tax	3	382	258
U.S. tax (benefit) cost of foreign earnings	(12)	(467)	54
Foreign tax rate differential	(2,202)	(2,802)	(1,632)
Extraterritorial income exclusion	–	(33)	(23)
Change in valuation allowance	14,514	17	242
Nondeductible expenses	1,339	542	727
Research and development tax credits	(419)	(144)	(145)
Other	76	(144)	(325)
	$ 8,466	$ 9,784	$ 8,688

Notes to Consolidated Financial Statements

5. Income Taxes (continued)

Net deferred tax liability in the accompanying consolidated balance sheet consists of the following:

(In thousands)	2008	2007
Deferred Tax Asset (Liability):		
Reserves and accruals	$ 8,954	$ 8,082
Foreign and alternative minimum tax credits	7,767	6,923
Research and development	3,656	2,330
Operating loss carryforwards	2,660	5,072
Inventory basis difference	1,592	772
Employee compensation	1,402	683
Allowance for doubtful accounts	654	192
Other	129	55
Deferred Tax Asset, Gross	26,814	24,109
Less: Valuation Allowance	(19,110)	(2,696)
Deferred Tax Asset, Net	7,704	21,413
Goodwill and intangible assets	(7,976)	(19,562)
Fixed assets basis difference	(3,140)	(3,281)
Revenue recognition	(982)	(369)
Reserves and accruals	(543)	(707)
Other	(71)	(218)
Deferred Tax Liability	(12,712)	(24,137)
Net Deferred Tax Liability	$ (5,008)	$ (2,724)

The deferred tax asset and liability are presented in the accompanying balance sheet within other current assets, other assets, other current liabilities and deferred income taxes based on when the tax benefits are expected to be realized and on a net basis by tax jurisdiction.

The Company has established valuation allowances related to certain domestic and foreign deferred tax assets and tax credits. The valuation allowance at year-end 2008 was $19,110,000. The increase in the valuation allowance in 2008 of $16,414,000 related primarily to applying a valuation allowance against certain deferred tax assets, including foreign tax credit carryforwards. Compliance with SFAS 109 requires the Company to periodically evaluate the necessity of establishing or adjusting a valuation allowance for deferred tax assets depending on whether it is more likely than not that a related tax benefit will be recognized in future periods. As a result of the accumulated loss position in the U.S. tax jurisdiction at January 3, 2009 and the uncertainty of profitability in future periods, the Company has recorded a valuation allowance.

At year-end 2008, the Company had domestic federal, state, and foreign net operating loss carryforwards of $3,088,000, $9,923,000 and $7,385,000, respectively, and U.S. foreign tax credits of $6,498,000. The domestic federal net operating loss carryforwards will expire in the years 2025 through 2026 and the domestic state loss carryforwards will expire in the years 2009 through 2028. Their use is limited to future taxable earnings from the Company's domestic subsidiaries. Of the foreign net operating loss carryforwards, $5,788,000 expire in the years 2009 through 2028, and the remainder do not expire. The U.S. foreign tax credits expire beginning in 2012.

The Company has not recognized a deferred tax liability for the difference between the book basis and the tax basis of its investment in the stock of its domestic subsidiaries, related primarily to unremitted earnings of

Notes to Consolidated Financial Statements

5. Income Taxes (continued)

subsidiaries, because it does not expect this basis difference to become subject to tax at the parent level. The Company believes it can implement certain tax strategies to recover its investment in its domestic subsidiaries tax-free.

It is the Company's practice to reinvest indefinitely the earnings of its international subsidiaries, except in instances in which the Company can remit such earnings without a significant associated tax cost. Through year-end 2008, the Company has not provided U.S. income taxes on approximately $98,100,000 of unremitted foreign earnings. The U.S. tax cost has not been determined as it is not practicable to estimate at this time. The related foreign tax withholding, which would be required if the Company remitted the foreign earnings to the U.S., would be approximately $5,700,000.

The Company has two subsidiaries located in China that have a tax holiday, which reduces the income tax in that country. The tax holiday began in 2007 for each company and will expire in 2011. Based on the currently enacted regular corporate income tax rate in China, the benefit to the Company of the tax holiday for year-end 2008 was approximately $121,000, or $.01 per diluted share.

The Company operates within multiple tax jurisdictions and could be subject to audit in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve and may cover multiple years. In management's opinion, adequate provisions for income taxes have been made for all years subject to audit.

A tabular reconciliation of the beginning and ending amount of unrecognized tax benefits at year-end 2008 and 2007 is as follows:

(In thousands)	2008	2007
Unrecognized tax benefits, beginning of year	$4,040	$4,069
Gross increases—tax positions in prior periods	1	–
Gross decreases—tax positions in prior periods	(171)	(1)
Gross increases—current-period tax positions	1,691	601
Settlements	(249)	(32)
Lapses of statutes of limitation	(196)	(597)
Unrecognized tax benefits, end of year	$5,116	$4,040

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. The Company has accrued $1,426,000 and $1,309,000 for the potential payment of interest and penalties at year-end 2008 and 2007, respectively. The interest and penalties reflected in the statement of operations in 2008 and 2007 were approximately $117,000 and $13,000, respectively. The total liabilities associated with unrecognized tax benefits that, if recognized, would impact the annual effective tax rate were approximately $2,440,000 in 2008.

The Company does not anticipate that the total amount of unrecognized tax benefit related to any particular tax position will change significantly within the next 12 months.

As of year-end 2008, the Company was subject to U.S. Federal income tax examinations for the stub period from January to August 2001 when the Company was part of its former parent company's tax return and for the tax years 2005 through 2008, and to non-U.S. income tax examinations for the tax years 2001 through 2008. In addition, the Company was subject to state and local income tax examinations for the tax years 2004 through 2008.

Notes to Consolidated Financial Statements

6. Short- and Long-Term Obligations and Other Financing Arrangements

Short- and long-term obligations at year-end 2008 and 2007 are as follows:

(In thousands)	2008	2007
Revolving Credit Facility	$38,000	$ –
Variable Rate Term Loan, due from 2008 to 2010	–	25,974
Variable Rate Term Loan, due from 2009 to 2016	8,750	9,250
Variable Rate Term Loan, due from 2010 to 2011	5,872	5,476
Short-Term Obligation under Kadant Jining 2008 Facilities	2,789	–
Total Short- and Long-Term Obligations	55,411	40,700
Less: Short-Term Obligations and Current Maturities	(3,289)	(10,240)
Long-Term Obligations, less Current Maturities	$52,122	$ 30,460

The annual payment requirements for short- and long-term obligations are as follows:

(In thousands)	
2009	$ 3,289
2010	4,023
2011	2,849
2012	500
2013	38,500
2014 and thereafter	6,250

The weighted average interest rate for short- and long-term obligations was 4.26% and 5.57% at year-end 2008 and 2007, respectively.

Revolving Credit Facility

On February 13, 2008, the Company entered into a five-year unsecured revolving credit facility (2008 Credit Agreement) in the aggregate principal amount of up to $75,000,000, which includes an uncommitted unsecured incremental borrowing facility of up to an additional $75,000,000. The Company borrowed $20,000,000 under the 2008 Credit Agreement and applied the proceeds to repay a portion of its term loan and revolving credit facility (2005 Credit Agreement). The Company used available cash of $5,974,000 to repay the balance of its outstanding debt under the 2005 Credit Agreement, which was then terminated. The Company can borrow up to $75,000,000 under the 2008 Credit Agreement with a sublimit of $60,000,000 within the 2008 Credit Agreement available for the issuance of letters of credit and bank guarantees. The principal on any borrowings made under the 2008 Credit Agreement is due on February 13, 2013. Interest on any loans outstanding under the 2008 Credit Agreement accrues and is payable quarterly in arrears at one of the following rates selected by the Company: (a) the prime rate plus an applicable margin (up to .20%) or (b) a Eurocurrency rate plus an applicable margin (up to 1.20%). The applicable margin is determined based upon the Company's total debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio. As of January 3, 2009, the outstanding balance on the 2008 Credit Agreement was $38,000,000. The amount the Company is able to borrow under the 2008 Credit Agreement is the total borrowing capacity less any outstanding borrowings, letters of credit and multi-currency borrowings issued under the 2008 Credit Agreement. As of January 3, 2009, the Company had $33,474,000 of borrowing capacity available under the committed portion of the 2008 Credit Agreement.

6. Short- and Long-Term Obligations and Other Financing Arrangements (continued)

The obligations of the Company under the 2008 Credit Agreement may be accelerated upon the occurrence of an event of default under the 2008 Credit Agreement, which includes customary events of default including, without limitation, payment defaults, defaults in the performance of affirmative and negative covenants, the inaccuracy of representations or warranties, bankruptcy and insolvency related defaults, defaults relating to such matters as the Employment Retirement Income Security Act (ERISA), uninsured judgments and the failure to pay certain indebtedness, and a change of control default.

The loans under the 2008 Credit Agreement are guaranteed by certain domestic subsidiaries of the Company pursuant to the Guarantee Agreement effective as of February 13, 2008. In addition, the 2008 Credit Agreement contains negative covenants applicable to the Company and its subsidiaries, including financial covenants requiring the Company to comply with a maximum consolidated leverage ratio of 3.5 and a minimum consolidated fixed charge coverage ratio of 1.2, and restrictions on liens, indebtedness, fundamental changes, dispositions of property, making certain restricted payments (including dividends and stock repurchases), investments, transactions with affiliates, sale and leaseback transactions, swap agreements, changing its fiscal year, arrangements affecting subsidiary distributions, entering into new lines of business, and certain actions related to the discontinued operation. As of January 3, 2009, the Company was in compliance with these covenants.

2006 Commercial Real Estate Loan

On May 4, 2006, the Company borrowed $10,000,000 under a promissory note (2006 Commercial Real Estate Loan), which is repayable in quarterly installments of $125,000 over a ten-year period with the remaining principal balance of $5,000,000 due upon maturity. Interest on the 2006 Commercial Real Estate Loan accrues and is payable quarterly in arrears at one of the following rates selected by the Company: (a) the prime rate or (b) the three-month London Inter-Bank Offered Rate (LIBOR) plus a 1% margin. Effective February 14, 2008, this margin was lowered to .75%. The 2006 Commercial Real Estate Loan is guaranteed and secured by real estate and related personal property of the Company and certain of its domestic subsidiaries, located in Theodore, Alabama; Auburn, Massachusetts; Three Rivers, Michigan; and Queensbury, New York, pursuant to mortgage and security agreements dated May 4, 2006 (Mortgage and Security Agreements). As of January 3, 2009, the remaining balance on the 2006 Commercial Real Estate Loan was $8,750,000.

The Company’s obligations under the 2006 Commercial Real Estate Loan may be accelerated upon the occurrence of an event of default under the 2006 Commercial Real Estate Loan and the Mortgage and Security Agreements, which include customary events of default including without limitation payment defaults, defaults in the performance of covenants and obligations, the inaccuracy of representations or warranties, bankruptcy- and insolvency-related defaults, liens on the properties or collateral and uninsured judgments. In addition, the occurrence of an event of default under the 2008 Credit Agreement or any successor credit facility would be an event of default under the 2006 Commercial Real Estate Loan.

2008 Kadant Jining Loan and Credit Facilities

On January 28, 2008, the Company’s Kadant Jining subsidiary (Kadant Jining) borrowed 40 million Chinese renminbi, or approximately $5,872,000 at the January 3, 2009 exchange rate (2008 Kadant Jining Loan). Principal on the 2008 Kadant Jining Loan is due as follows: 24 million Chinese renminbi, or approximately $3,523,000, on January 28, 2010 and 16 million Chinese renminbi, or approximately $2,349,000, on January 28, 2011. Interest on the 2008 Kadant Jining Loan accrues and is payable quarterly in arrears based on 95% of the interest rate published by The People’s Bank of China for a loan of the same term. The proceeds from the 2008

Notes to Consolidated Financial Statements

6. Short- and Long-Term Obligations and Other Financing Arrangements (continued)

Kadant Jining Loan were used to repay outstanding debt totaling 40 million Chinese renminbi, or $5,476,000 at year-end 2007.

On July 30, 2008, Kadant Jining and the Company's Kadant Yanzhou subsidiary (Kadant Yanzhou) each entered into a short-term credit line facility agreement (2008 Facilities) that would allow Kadant Jining to borrow up to an aggregate principal amount of 45 million Chinese renminbi, or approximately $6,606,000 at the January 3, 2009 exchange rate, and Kadant Yanzhou to borrow up to an aggregate principal amount of 15 million Chinese renminbi, or approximately $2,202,000 at the January 3, 2009 exchange rate. The 2008 Facilities have a term of 364 days and are renewable annually on or before July 30 at the discretion of the lender. Borrowings made under the 2008 Facilities will bear interest at the applicable short-term interest rate for a Chinese renminbi loan of comparable term as published by The People's Bank of China and will be used for general working capital purposes. The Company has provided a parent guaranty securing the payment of all obligations made under the 2008 Facilities and the 2008 Kadant Jining Loan and providing a cross-default to the Company's other senior indebtedness, including the 2008 Credit Agreement. As of January 3, 2009, Kadant Jining had borrowed $2,789,000 and Kadant Jining and Yanzhou had $6,019,000 of borrowing capacity available under the 2008 Facilities.

Debt Issuance Costs

Debt issuance costs are being amortized to interest expense over the corresponding debt term based on the effective-interest method. As of January 3, 2009, unamortized debt issuance costs were approximately $549,000.

Derivative Instruments

To hedge the exposure to movements in the 3-month LIBOR rate on future outstanding debt, on February 13, 2008, the Company entered into a swap agreement (2008 Swap Agreement). The 2008 Swap Agreement has a five-year term and a $15,000,000 notional value, which decreases to $10,000,000 on December 31, 2010, and $5,000,000 on December 30, 2011. Under the 2008 Swap Agreement, on a quarterly basis the Company will receive a 3-month LIBOR rate and pay a fixed rate of interest of 3.265% plus the applicable margin.

The Company entered into a swap agreement in 2006 (2006 Swap Agreement) to convert the 2006 Commercial Real Estate Loan from a floating to a fixed rate of interest. The 2006 Swap Agreement has the same terms and quarterly payment dates as the corresponding debt, and reduces proportionately in line with the amortization of the debt.

The 2006 and 2008 Swap Agreements have been designated as cash flow hedges and are carried at fair value with unrealized gains or losses reflected within other comprehensive items. As of January 3, 2009, the unrealized loss associated with the 2006 and 2008 Swap Agreements was $2,105,000 included in other liabilities, with an offset to accumulated other comprehensive items (net of tax) in the accompanying consolidated balance sheet. Management believes that any credit risk associated with the 2006 and 2008 Swap Agreements is remote based on the Company's financial position and the creditworthiness of the financial institution issuing the 2006 and 2008 Swap Agreements.

The Company uses forward currency-exchange contracts primarily to hedge certain operational exposures resulting from fluctuations in currency exchange rates. Such exposures primarily result from portions of the Company's operations and assets that are denominated in currencies other than the functional currencies of the businesses conducting the operations or holding the assets. The gains and losses resulting from foreign curency-exchange contracts that are not designated as hedges for accounting purposes are included in selling, general and

6. Short- and Long-Term Obligations and Other Financing Arrangements (continued)

administrative expenses in the accompanying consolidated statement of operations. The Company had a gain of $969,000 in 2008 and a loss of $83,000 in 2007 related to these foreign currency-exchange contracts. For forward currency-exchange contracts which have been designated as cash flow hedges, the unrealized gains and losses are included in accumulated other comprehensive items. As of January 3, 2009, the net receivable associated with forward currency-exchange contracts was $1,259,000, of which $1,329,000 is included in other current assets and $70,000 is included in other current liabilities, with an offset to accumulated other comprehensive items (net of tax) in the accompanying consolidated balance sheet. Management believes that any credit risk associated with these contracts is remote based on the Company's financial position and the creditworthiness of the financial institutions issuing the contracts.

7. Commitments and Contingencies

Operating Leases

The Company occupies office and operating facilities under various operating leases. The accompanying consolidated statement of operations includes expenses from operating leases of $2,927,000, $2,911,000, and $2,760,000 in 2008, 2007, and 2006, respectively. The future minimum payments due under noncancelable operating leases as of January 3, 2009, are $1,999,000 in 2009; $1,420,000 in 2010; $977,000 in 2011; $658,000 in 2012; $279,000 in 2013 and $20,000 thereafter. Total future minimum lease payments are $5,353,000.

Letters of Credit

Outstanding letters of credit issued on behalf of the Company as applicant, principally relating to performance obligations and customer deposit guarantees, totaled $20,785,000 at January 3, 2009. Certain of the Company's contracts, particularly for stock-preparation and systems orders, require the Company to provide a standby letter of credit to a customer as beneficiary, limited in amount to a negotiated percentage of the total contract value, in order to guarantee warranty and performance obligations of the Company under the contract. Typically, these standby letters of credit expire without being drawn by the beneficiary. The Company could incur an additional cost if a beneficiary draws upon such a standby letter of credit. See *Letters of Credit* in Note 15 for further information.

In connection with the Kadant Johnson acquisition, the Company issued a letter of credit to the sellers for $3,381,000 related to additional cash consideration the Company expects to pay through 2010.

Contingencies

In the ordinary course of business, the Company is, at times, required to issue limited performance guarantees, some of which do not require the issuance of letters of credit to customers in support of these guarantees, relating to its equipment and systems. The Company typically limits its liability under these guarantees to amounts that would not exceed the value of the contract. The Company believes that it has adequate reserves for any potential liability in connection with such guarantees.

Notes to Consolidated Financial Statements

7. Commitments and Contingencies (continued)

Litigation

The Company has been named as a co-defendant, together with Composites LLC and another defendant, in a consumer class action lawsuit filed in the United States District Court for the District of Massachusetts (the Court) on December 27, 2007 on behalf of a putative class of individuals who own GeoDeck™ decking or railing products manufactured by Composites LLC between April 2002 and October 2003. The complaint in this matter purports to assert, among other things, causes of action for unfair and deceptive trade practices, fraud, negligence, breach of warranty and unjust enrichment, and it seeks compensatory damages and punitive damages under various state consumer protection statutes, which plaintiffs claim exceed $50 million. On March 14, 2008, the Company, Composites LLC, and the other co-defendant filed motions to dismiss all counts in the complaint. On November 19, 2008, the Court dismissed the complaint in its entirety, including all claims against the Company, Composites LLC, and the other co-defendant. On December 4, 2008, the plaintiffs sought to vacate this order of dismissal in order to amend their complaint, and this motion was denied without prejudice by the Court on January 12, 2009. On January 27, 2009, the plaintiffs renewed their motion to vacate the order of dismissal in order to file an amended complaint, which motion was denied by the Court on March 3, 2009. The plaintiffs have not indicated whether they will attempt to appeal the Court's order. The Company intends to defend against this action vigorously, but there is no assurance the Company will prevail in such defense. The Company could incur significant costs to defend this lawsuit and a judgment or a settlement of the claims against the defendants could have a material adverse impact on the Company's consolidated financial results.

Indemnification

The Company is required to indemnify Thermo Electron, but not its shareholders, against liability for taxes arising from the Company's conduct of business after the spin-off, or the failure of certain distributions to continue to qualify as a tax free spin-off, as described in Note 1 "Income Taxes."

8. Restructuring Costs (Income) and Other Income, Net

Other Income

In 2008, the Company sold real estate in France for $746,000, resulting in a pre-tax gain of $594,000, as well as, real estate in the United Kingdom for $1,903,000, resulting in a pre-tax gain of $1,093,000.

2006 Restructuring Plan

The Company recorded restructuring costs of $677,000 in 2006 associated with its 2006 Restructuring Plan. These restructuring costs comprised severance and associated costs related to the reduction of 15 full-time positions in Canada and France, all in its Papermaking Systems segment. The Company recorded restructuring costs of $252,000 in 2007 associated with exit costs related to vacating a facility in Canada. In addition, in 2008 and 2007, the Company reduced the restructuring reserve for the 2006 Restructuring Plan by $105,000 and $276,000, respectively, as the reserve was no longer required.

Notes to Consolidated Financial Statements

8. Restructuring Costs (Income) and Other Income, Net (continued)

2008 Restructuring Plan

The Company recorded restructuring costs of $3,802,000 in 2008 associated with its 2008 Restructuring Plan. These restructuring costs included severance and associated costs related to the reduction of 329 full-time positions in China, the U.S., Latin America, Canada, and Sweden, all at its Papermaking Systems segment. These actions were taken to adjust the Company's cost structure and streamline its operations in response to the weak economic environment, which accelerated in the fourth quarter of 2008, and its negative impact on current and projected order volumes, especially in its stock-preparation equipment product line.

A summary of the changes in accrued restructuring costs, of which $2,256,000 is included in other current liabilities and $616,000 is included in other long-term liabilities in the accompanying consolidated balance sheet, are as follows:

(In thousands)	Severance Costs
2006 Restructuring Plan	
Provision	$ 677
Usage	(65)
Currency translation	(6)
Balance at December 30, 2006	$ 606
Provision	252
Reserve reduction	(276)
Usage	(372)
Currency translation	98
Balance at December 29, 2007	$ 308
Reserve reduction	(105)
Usage	(195)
Currency translation	(8)
Balance at January 3, 2009	$ –
2008 Restructuring Plan	
Provision	$ 3,802
Usage	(879)
Currency translation	(51)
Balance at January 3, 2009	$ 2,872

The Company expects to pay the remaining accrued restructuring costs as follows: $2,256,000 in 2009 and $616,000 from 2010 to 2015.

Notes to Consolidated Financial Statements

9. Discontinued Operation

On October 21, 2005, Composites LLC sold substantially all of its assets to LDI Composites Co. (Buyer) for approximately $11,913,000 in cash and the assumption of $658,000 of liabilities, resulting in a cumulative loss on sale of $84,000. Under the terms of the asset purchase agreement, Composites LLC retained certain liabilities associated with the operation of the business prior to the sale, including the warranty obligations associated with products manufactured prior to the sale date. Composites LLC retained all of the cash proceeds received from the asset sale and continued to administer and pay warranty claims from the sale proceeds into the third quarter of 2007. On September 30, 2007, Composites LLC announced that it no longer had sufficient funds to honor warranty claims, was unable to pay or process warranty claims, and ceased doing business. All activity related to this business is classified in the results of the discontinued operation in the accompanying consolidated financial statements.

Operating results for the composites business included in the results of the discontinued operation in the accompanying consolidated statement of operations are as follows:

(In thousands)	2008	2007	2006
Operating Loss	$ (28)	$(4,332)	$(2,204)
Interest Income	–	74	318
Loss Before Income Tax Benefit (including $130 loss on disposal in 2006)	(28)	(4,258)	(1,886)
Income Tax Benefit	65	1,508	702
Income (Loss) from Discontinued Operation	$ 37	$(2,750)	$(1,184)

The major classes of assets and liabilities of the composites business included in the discontinued operation in the accompanying consolidated balance sheet are as follows:

(In thousands)	2008	2007
Cash and Cash Equivalents	$ 2	$ 3
Other Accounts Receivable	322	322
Deferred Tax Asset	–	769
Other Assets	200	199
Total Assets	524	1,293
Accounts Payable	255	255
Accrued Warranty Costs	2,142	2,142
Other Current Liabilities	30	31
Total Liabilities	2,427	2,428
Net Liabilities	$(1,903)	$(1,135)

As part of the sale transaction, Composites LLC retained the warranty obligations associated with products manufactured prior to the sale date. Through the sale date of October 21, 2005, Composites LLC offered a standard limited warranty to the owner of its decking and roofing products, limited to repair or replacement of the defective product or a refund of the original purchase price.

9. Discontinued Operation (continued)

Through the second quarter of 2006, Composites LLC recorded an estimate for warranty-related costs at the time of sale based on its actual historical return rates and repair costs, as well as other analytical tools for estimating future warranty claims. These estimates were revised for variances between actual and expected claims rates. Composites LLC's analysis of expected warranty claims rates included detailed assumptions associated with potential product returns, including the type of product sold, temperatures at the location of installation, density of boards, and other factors. Certain assumptions, such as the effect of weather conditions and high temperatures on the product installed, included inherent uncertainties that contributed to variances between actual and expected claims rates.

During the third quarter of 2006, Composites LLC concluded that the assumptions noted above were not accurately predicting the actual level of warranty claims, making it no longer possible to calculate a reasonable estimate of the future level of potential warranty claims. Accordingly, as no amount within the total range of loss represents a best estimate of the ultimate loss to be recorded, Composites LLC is required under SFAS 5 to record the minimum amount of the potential range of loss for products under warranty. As of January 3, 2009, the accrued warranty costs associated with the composites business were $2,142,000, which represents the low end of the estimated range of warranty reserve required based on the level of claims received through the end of 2008. Composites LLC has calculated that the total potential warranty cost ranges from $2,142,000 to approximately $13,100,000. The high end of the range represents the estimated maximum level of warranty claims remaining based on the total sales of the products under warranty. Composites LLC will continue to record adjustments to the accrued warranty costs to reflect the minimum amount of the potential range of loss for products under warranty based on judgments entered against it in litigation, if any.

The changes in the carrying amount of accrued warranty costs are as follows:

(In thousands)	2008	2007
Balance at Beginning of Year	$ 2,142	$ 1,135
Provision charged to income	–	3,914
Usage	–	(2,907)
Balance at End of Year	$ 2,142	$ 2,142

See *Litigation* in Note 7 for information related to pending litigation associated with the composites business.

10. Fair Value Measurements

The Company adopted SFAS No. 157, "Fair Value Measurements" (SFAS 157), on December 30, 2007, which did not have a material impact on the Company's fair value measurements. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. SFAS 157 establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair value into three broad levels as follows:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
- Level 2—Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly.
- Level 3—Unobservable inputs based on the Company's own assumptions.

Notes to Consolidated Financial Statements

10. Fair Value Measurements (continued)

The following table presents the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of January 3, 2009:

	Fair Value			
(In thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets:				
Forward currency-exchange contracts	$ –	$1,329	$ –	$1,329
Liabilities:				
Forward currency-exchange contracts	$ –	$ 70	$ –	$ 70
Interest-rate swap agreements	$ –	$2,105	$ –	$2,105

The Company uses the market approach technique to value its financial assets and liabilities and there were no changes in valuation techniques during 2008. The Company's financial assets and liabilities carried at fair value primarily comprise derivative instruments used to hedge the Company's foreign currency and interest rate risks. The fair values of the Company's interest-rate swap agreements are based on LIBOR yield curves at the reporting date. The fair values of the Company's forward currency-exchange contracts are based on quoted forward foreign exchange prices at the reporting date. The forward currency-exchange contracts and interest rate swap agreements are hedges of either recorded assets or liabilities or anticipated transactions. Changes in values of the underlying hedged assets and liabilities or anticipated transactions are not reflected in the table above.

11. Business Segment and Geographical Information

The Company has combined its operating entities into one reportable operating segment, Papermaking Systems, and two separate product lines, which are reported in Other, Fiber-based Products and Casting Products, the latter of which was sold on April 30, 2007. In classifying operational entities into a particular segment, the Company aggregated businesses with similar economic characteristics, products and services, production processes, customers, and methods of distribution.

The Company's Papermaking Systems segment develops, manufactures, and markets stock-preparation systems and equipment, paper machine accessory equipment, water-management systems, and fluid-handling systems and equipment for the pulp and paper industry worldwide. Principal products manufactured by this segment include: custom-engineered systems and equipment for the preparation of wastepaper for conversion into recycled paper; fluid-handling systems used primarily in the dryer section of the papermaking process and during the production of corrugated boxboard, metals, plastics, rubber, textiles, and food; paper machine accessory equipment and related consumables important to the efficient operation of paper machines; and water-management systems essential for draining, purifying, and recycling process water. The Fiber-based Products line produces biodegradable absorbent granules from papermaking byproducts. These granules are primarily used as carriers for agricultural, home lawn and garden, and professional lawn, turf and ornamental applications, as well as for oil and grease absorption. The Casting Products line produced grey and ductile iron castings through its sale on April 30, 2007.

Notes to Consolidated Financial Statements

11. Business Segment and Geographical Information (continued)

(In thousands)	2008	2007	2006
Business Segment Information			
Revenues:			
Papermaking Systems (a)	$321,747	$356,334	$327,501
Other (b)	7,411	10,162	14,112
	$329,158	$366,496	$341,613
Revenues by Product Line:			
Papermaking Systems:			
Stock-Preparation Equipment	$128,254	$165,820	$146,275
Fluid-Handling	98,675	93,970	84,388
Accessories	60,715	63,128	60,588
Water-Management	31,687	31,083	33,787
Other	2,416	2,333	2,463
	$321,747	$356,334	$327,501
Other (b):			
Fiber-based Products	$ 7,411	$ 8,689	$ 10,124
Casting Products	–	1,473	3,988
	$ 7,411	$ 10,162	$ 14,112
(Loss) Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense:			
Papermaking Systems (c)(d)	$ 1,341	$ 49,128	$ 38,604
Corporate and Other (b)	(14,348)	(12,090)	(9,162)
Total operating (loss) income	(13,007)	37,038	29,442
Interest expense, net	(803)	(1,516)	(2,207)
	$ (13,810)	$ 35,522	$ 27,235
Total Assets:			
Papermaking Systems	$342,785	$427,996	$385,842
Corporate and Other (b,e)	13,608	7,780	2,782
Total Assets from Continuing Operations	356,393	435,776	388,624
Total Assets from Discontinued Operation	524	1,293	4,461
	$356,917	$437,069	$393,085
Depreciation and Amortization:			
Papermaking Systems	$ 7,037	$ 6,845	$ 7,171
Corporate and Other (b)	493	518	587
	$ 7,530	$ 7,363	$ 7,758
Capital Expenditures:			
Papermaking Systems	$ 5,606	$ 4,436	$ 3,579
Corporate and Other (b)	592	472	518
	$ 6,198	$ 4,908	$ 4,097

Notes to Consolidated Financial Statements

11. Business Segment and Geographical Information (continued)

(In thousands)	2008	2007	2006
Geographical Information			
Revenues (f):			
United States	$166,236	$221,573	$210,499
France	69,078	61,006	61,261
China	41,594	35,227	20,119
Other	87,237	83,497	75,368
Transfers among geographic areas (g)	(34,987)	(34,807)	(25,634)
	$329,158	$366,496	$341,613
Long-lived Assets (h):			
United States	$ 18,546	$ 17,073	$ 18,358
China	13,585	12,984	11,716
Other	9,507	11,847	11,581
	$ 41,638	$ 41,904	$ 41,655
Export Revenues Included in United States Revenues Above (i)	$ 30,463	$ 69,570	$ 69,449

(a) Revenues from China were $44.2 million, $76.6 million, and $71.3 million in 2008, 2007, and 2006, respectively.
(b) "Other" includes the results from the Fiber-based Products business and the Casting Products business through its sale on April 30, 2007.
(c) Includes a goodwill impairment charge of $40.3 million in 2008 (see Note 1).
(d) Includes restructuring costs (income) and other income, net, of $2.0 million, ($0.2) million, and $0.8 million in 2008, 2007, and 2006, respectively (see Note 8).
(e) Primarily includes cash and cash equivalents and property, plant, and equipment.
(f) Revenues are attributed to countries based on selling location.
(g) Transfers among geographic areas are accounted for at prices that are representative of transactions with unaffiliated parties.
(h) Primarily includes property, plant, and equipment, net.
(i) In general, export revenues are denominated in U.S. dollars.

12. (Loss) Earnings per Share

Basic and diluted (loss) earnings per share were calculated as follows:

(In thousands, except per share amounts)	2008	2007	2006
(Loss) Income from Continuing Operations	$(22,595)	$25,418	$18,281
Income (Loss) from Discontinued Operation	37	(2,750)	(1,184)
Net (Loss) Income	$(22,558)	$22,668	$17,097
Basic Weighted Average Shares	13,527	14,116	13,816
Effect of Stock Options, Restricted Stock Awards and Employee Stock Purchase Plan	–	174	281
Diluted Weighted Average Shares	13,527	14,290	14,097
Basic (Loss) Earnings per Share:			
Continuing Operations	$ (1.67)	$ 1.80	$ 1.32
Discontinued Operation	–	(.19)	(.08)
Net (Loss) Income per Basic Share	$ (1.67)	$ 1.61	$ 1.24
Diluted (Loss) Earnings per Share:			
Continuing Operations	$ (1.67)	$ 1.78	$ 1.30
Discontinued Operation	–	(.19)	(.09)
Net (Loss) Income per Diluted Share	$ (1.67)	$ 1.59	$ 1.21

Options to purchase 60,300 shares, 57,200 shares, and 116,000 shares of common stock were not included in the computation of diluted (loss) earnings per share for 2008, 2007, and 2006, respectively, because the options' exercise prices were greater than the average market price for the common stock, and the effect would have been antidilutive. In addition, the dilutive effect of options and restricted stock units totaling 104,400 shares of common stock were not included in the computation of diluted (loss) earnings per share in 2008 as the effect would have been antidilutive.

13. Accumulated Other Comprehensive Items

Comprehensive income combines net (loss) income and other comprehensive items, which represent certain amounts that are reported as components of shareholders' investment in the accompanying consolidated balance sheet, including foreign currency translation adjustments, deferred losses, unrecognized transition obligation and unrecognized prior service income associated with pension and other post-retirement plans, and deferred gains and losses on hedging instruments.

Accumulated other comprehensive items in the accompanying consolidated balance sheet consist of the following:

(In thousands)	2008	2007
Cumulative Translation Adjustment	$ 2,106	$16,967
Unrecognized Prior Service Income	259	682
Deferred Loss on Pension and Other Post-Retirement Plans	(6,901)	(1,812)
Deferred (Loss) Gain on Hedging Instruments	(1,649)	66
Unrecognized Transition Obligation	(3)	(5)
	$(6,188)	$15,898

14. Unaudited Quarterly Information

2008 (In thousands, except per share amounts)	First	Second	Third	Fourth
Revenues	$ 85,864	$ 92,406	$ 83,734	$ 67,154
Gross Profit	34,060	38,563	34,267	28,913
Income (Loss) from Continuing Operations (a)	5,117	6,893	6,835	(41,440)
(Loss) Income from Discontinued Operation	(4)	(5)	23	23
Net Income (Loss)	$ 5,113	$ 6,888	$ 6,858	$ (41,417)
Basic Earnings (Loss) per Share:				
Continuing Operations	$ .36	$ .50	$ .51	$ (3.25)
Net Income (Loss)	$ .36	$ .50	$ .51	$ (3.25)
Diluted Earnings (Loss) per Share:				
Continuing Operations	$ .36	$ .50	$ .50	$ (3.25)
Net Income (Loss)	$ .36	$ .50	$ .50	$ (3.25)

2007 (In thousands, except per share amounts)	First	Second	Third	Fourth
Revenues	$ 88,241	$ 89,107	$ 92,695	$ 96,453
Gross Profit	32,547	34,143	35,338	36,752
Income from Continuing Operations	4,691	5,936	7,013	7,778
Loss from Discontinued Operation	(392)	(1,022)	(1,232)	(104)
Net Income	$ 4,299	$ 4,914	$ 5,781	$ 7,674
Basic Earnings per Share:				
Continuing Operations	$ .33	$ .42	$ .49	$ .54
Discontinued Operation	(.02)	(.07)	(.08)	–
Net Income per Basic Share	$ .31	$ .35	$ .41	$ .54
Diluted Earnings per Share:				
Continuing Operations	$ .33	$ .42	$ .49	$ .54
Discontinued Operation	(.03)	(.07)	(.09)	(.01)
Net Income per Diluted Share	$ .30	$ .35	$ .40	$ .53

(a) Includes a $40.3 million pre-tax goodwill impairment charge, a $15.4 million tax provision associated with applying a valuation allowance to certain deferred tax assets, and a $3.1 million pre-tax restructuring charge in the fourth quarter of 2008.

Notes to Consolidated Financial Statements

15. Subsequent Event

Letters of Credit

Certain of the Company's contracts, particularly for stock-preparation and systems orders, require the Company to provide a standby letter of credit to a customer as beneficiary, limited in amount to a negotiated percentage of the total contract value, in order to guarantee warranty and performance obligations of the Company under the contract. Typically, these standby letters of credit expire without being drawn by the beneficiary. In the first quarter of 2009, one of the Company's customers in China indicated its intention to draw upon all outstanding standby letters of credit issued to the customer as beneficiary to secure warranty and performance obligations under multiple contracts. The Company believes the attempted draws by the customer are for reasons unrelated to the Company's warranty and performance obligations and the Company has and intends to continue to vigorously oppose such actions. To date, the customer has submitted draws against standby letters of credit totaling $421,000, and the Company has obtained a preliminary injunction against payment to the customer. The outstanding standby letters of credit to such customer, including those that have been submitted for draws, total $6,094,000 and have expiration dates from 2009 through 2011.

Kadant Inc.
Schedule II
Valuation and Qualifying Accounts
(In thousands)

Description	Balance at Beginning of Year	Provision Charged to Expense	Accounts Recovered	Accounts Written Off	Other (a)	Balance at End of Year
Allowance for Doubtful Accounts						
Year Ended January 3, 2009	$ 2,639	$ 1,252	$ 8	$ (830)	$ (84)	$ 2,985
Year Ended December 29, 2007	$ 2,623	$ 216	$ 25	$ (432)	$ 207	$ 2,639
Year Ended December 30, 2006	$ 2,221	$ 725	$ –	$ (486)	$ 163	$ 2,623

Description	Balance at Beginning of Year	Provision (Income) Charged to Expense	Activity Charged to Reserve	Currency Translation	Balance at End of Year
Accrued Restructuring Costs (b)					
Year Ended January 3, 2009 (c)	$ 308	$ 3,697	$ (1,074)	$ (59)	$ 2,872
Year Ended December 29, 2007	$ 971	$ (219)	$ (580)	$ 136	$ 308
Year Ended December 30, 2006	$ 4,781	$ 815	$ (5,173)	$ 548	$ 971

(a) Primarily includes the effect of foreign currency translation.
(b) The nature of the activity in this account is described in Note 8 to the consolidated financial statements.
(c) Consists of $2.3 million in other current liabilities and $0.6 million in other long-term liabilities as of January 3, 2009.

Exhibit 10.2

AMENDED AND RESTATED EXECUTIVE RETENTION AGREEMENT

THIS AMENDED AND RESTATED EXECUTIVE RETENTION AGREEMENT by and between KĀDANT INC., a Delaware corporation (the "Company"), and **William A. Rainville** (the "Executive") is made as of December 9, 2008 (the "Effective Date").

WHEREAS, the Company and the Executive are parties to that certain Executive Retention Agreement dated as of August 8, 2001, as amended and restated effective as of December 5, 2006 (the "Original Agreement");

WHEREAS, the Board of Directors of the Company (the "Board") recognizes that, as is the case with many publicly-held corporations, the possibility of a change in control of the Company exists and that such possibility, and the uncertainty and questions which it may raise among key personnel, may result in the departure or distraction of key personnel to the detriment of the Company and its stockholders;

WHEREAS, the Board has determined that appropriate steps should be taken to reinforce and encourage the continued employment and dedication of the Company's key personnel without distraction from the possibility of a change in control of the Company and related events and circumstances; and

WHEREAS, the Board and the Executive intend that the Original Agreement comply with the provisions of Section 409A of the Internal Revenue Code (the "Code") and for that purpose desire to amend and restate the Original Agreement; and

NOW, THEREFORE, as an inducement for and in consideration of the Executive remaining in the Company's employ, the Executive and the Company agree as follows:

1. Key Definitions.

As used herein, the following terms shall have the following respective meanings:

1.1 "Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) (a "Person") of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 20% or more of either (i) the then-outstanding shares of common stock of the Company (the "Outstanding

Company Common Stock") or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this Section 1.1; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the Board of Directors of a successor corporation to the Company), where the term "Continuing Director" means at any date a member of the Board (i) who was a member of the Board on the date of the execution of this Agreement or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a "Business Combination"), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Company Common Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 80% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company's assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the "Acquiring Corporation") in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Company Common Stock and Outstanding Company Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 20% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

1.2 "Change in Control Date" means the first date during the Term (as defined in Section 2) on which a Change in Control occurs. Anything in this Agreement to the contrary notwithstanding, if (a) a Change in Control occurs, (b) the Executive's employment with the Company is terminated prior to the date on which the Change in Control occurs, and (c) it is reasonably demonstrated by the Executive that such termination of employment (i) was at the request of a third party who has taken steps reasonably calculated to effect a Change in Control or (ii) otherwise arose in connection with or in anticipation of a Change in Control, then for all purposes of this Agreement the "Change in Control Date" shall mean the date immediately prior to the date of such termination of employment.

1.3 "Cause" means the Executive's willful engagement in illegal conduct or gross misconduct after the Change in Control Date which is materially and demonstrably injurious to the Company. For purposes of this Section 1.3, no act or failure to act by the Executive shall be considered "willful" unless it is done, or omitted to be done, in bad faith and without reasonable belief that the Executive's action or omission was in the best interests of the Company.

1.4 "Good Reason" means the occurrence, without the Executive's written consent, of any of the events or circumstances set forth in clauses (a) through (g) below on or after the Change in Control Date. Notwithstanding the occurrence of any such event or circumstance, such occurrence shall not be deemed to constitute Good Reason if, prior to the Date of Termination specified in the Notice of Termination (each as defined in Section 3.2(a)) given by the Executive in respect thereof, such event or circumstance has been fully corrected within 30 days after notice thereof and the Executive has been reasonably compensated for any losses or damages resulting therefrom.

(a) the assignment to the Executive of duties inconsistent in any material respect with the Executive's position (including status, offices, titles and reporting requirements, including but not limited to a change in any of the foregoing that results in the Executive no longer being an officer of a public company), authority or responsibilities in effect immediately prior to the earliest to occur of (i) the Change in Control Date, (ii) the date of the execution by the Company of the initial written agreement or instrument providing for the Change in Control or (iii) the date of the adoption by the Board of Directors of a resolution providing for the Change in Control (with the earliest to occur of such dates referred to herein as the "Measurement Date") or a material diminution in such position, authority or responsibilities;

(b) a reduction in the Executive's annual base salary as in effect on the Measurement Date or as the same was or may be increased thereafter from time to time;

(c) the failure by the Company to (i) continue in effect any material compensation or benefit plan or program (including without limitation any life insurance, medical, health and accident or disability plan and any vacation or automobile program or policy) (a "Benefit Plan") in which the Executive participates or which is applicable to the Executive immediately prior to the Measurement Date, unless an equitable arrangement (embodied in an ongoing substitute or alternative plan) has been made with respect to such plan or program, (ii) continue the Executive's participation therein (or in such substitute or alternative plan) on a basis not materially less favorable than the basis existing immediately prior to the Measurement Date (iii) award cash bonuses to the Executive in amounts and in a manner substantially consistent with past practice in light of the Company's financial performance or (iv) continue to provide any material fringe benefit enjoyed by Executive immediately prior to the Measurement Date;

(d) a change by the Company in the location at which the Executive performs his or her principal duties for the Company to a new location that is both (i) outside a radius of 50 miles from the Executive's principal residence immediately prior to the Measurement Date and (ii) more than 30 miles from the location at which the Executive performed his or her principal duties for the Company immediately prior to the Measurement Date; or a requirement by the Company that the Executive travel on Company business to a substantially greater extent than required immediately prior to the Measurement Date;

(e) the failure of the Company to obtain the agreement from any successor to the Company to assume and agree to perform this Agreement, as required by Section 6.1;

(f) a material breach of this Agreement; or

(g) any failure of the Company to pay or provide to the Executive any portion of the Executive's compensation or benefits due under any Benefit Plan within seven days of the date such compensation or benefits are due, or any material breach by the Company of this Agreement or any employment agreement with the Executive.

The Executive's right to terminate his or her employment for Good Reason shall not be affected by the Executive's incapacity due to physical or mental illness.

1.5 "Disability" means the Executive's absence from the full-time performance of the Executive's duties with the Company for 180 consecutive calendar days as a result of incapacity due to mental or physical illness which is determined to be total and permanent by a physician selected by the Company or its insurers and acceptable to the Executive or the Executive's legal representative.

2. Term of Agreement. This Agreement, and all rights and obligations of the parties hereunder, shall take effect upon the Effective Date and shall expire upon the first

to occur of (a) the expiration of the Term (as defined below) if a Change in Control has not occurred during the Term, (b) the date 24 months after the Change in Control Date, if the Executive is still employed by the Company as of such later date, or (c) the fulfillment by the Company of all of its obligations under Sections 4 and 5.2 if the Executive's employment with the Company terminates within 24 months following the Change in Control Date. "Term" shall mean the period commencing as of the Effective Date and continuing in effect through December 31, 2011; provided, however, that commencing on January 1, 2012 and each January 1, thereafter, the Term shall be automatically extended for one additional year unless, not later than 90 days prior to the scheduled expiration of the Term (or any extension thereof), the Company shall have given the Executive written notice that the Term will not be extended.

3. Employment Status; Termination Following Change in Control.

3.1 Not an Employment Contract. The Executive acknowledges that this Agreement does not constitute a contract of employment or impose on the Company any obligation to retain the Executive as an employee and that this Agreement does not prevent the Executive from terminating employment at any time. If the Executive's employment with the Company terminates for any reason and subsequently a Change in Control shall occur, the Executive shall not be entitled to any benefits hereunder except as otherwise provided pursuant to Section 1.2.

3.2 Termination of Employment.

(a) If the Change in Control Date occurs during the Term, any termination of the Executive's employment by the Company or by the Executive within 24 months following the Change in Control Date (other than due to the death of the Executive) shall be communicated by a written notice to the other party hereto (the "Notice of Termination"), given in accordance with Section 7. Any Notice of Termination shall: (i) indicate the specific termination provision (if any) of this Agreement relied upon by the party giving such notice, (ii) to the extent applicable, set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of the Executive's employment under the provision so indicated and (iii) specify the Date of Termination (as defined below). The effective date of an employment termination (the "Date of Termination") shall be the close of business on the date specified in the Notice of Termination (which date may not be less than 15 days or more than 120 days after the date of delivery of such Notice of Termination), in the case of a termination other than one due to the Executive's death, or the date of the Executive's death, as the case may be. In the event the Company fails to satisfy the requirements of Section 3.2(a) regarding a Notice of Termination, the purported termination of the Executive's employment pursuant to such Notice of Termination shall not be effective for purposes of this Agreement.

(b) The failure by the Executive or the Company to set forth in the Notice of Termination any fact or circumstance which contributes to a showing of Good Reason or Cause shall not waive any right of the Executive or the Company, respectively, hereunder or preclude the Executive or the Company, respectively, from asserting any such fact or circumstance in enforcing the Executive's or the Company's rights hereunder.

(c) Any Notice of Termination for Cause given by the Company must be given within 90 days of the occurrence of the event(s) or circumstance(s) that constitute(s) Cause. Prior to any Notice of Termination for Cause being given (and prior to any termination for Cause being effective), the Executive shall be entitled to a hearing before the Board of Directors of the Company at which the Executive may, at the Executive's election, be represented by counsel and at which the Executive shall have a reasonable opportunity to be heard. Such hearing shall be held on not less than 15 days prior written notice to the Executive stating the Board of Directors' intention to terminate the Executive for Cause and stating in detail the particular event(s) or circumstance(s) that the Board of Directors believes constitutes Cause for termination.

(d) Any Notice of Termination for Good Reason given by the Executive must be given within 90 days of the first occurrence of the event(s) or circumstance(s) that constitute(s) Good Reason.

4. Benefits to Executive.

4.1 Stock Acceleration. If the Change in Control Date occurs during the Term, then, effective upon the Change in Control Date, (a) each outstanding option to purchase shares of Common Stock of the Company held by the Executive shall become immediately exercisable in full and will no longer be subject to a right of repurchase by the Company and (b) each outstanding restricted stock award shall be deemed to be fully vested and will no longer be subject to a right of repurchase by the Company.

4.2 Compensation. If the Change in Control Date occurs during the Term and the Executive's employment with the Company terminates within 24 months following the Change in Control Date, the Executive shall be entitled to the following benefits:

(a) Termination Without Cause or for Good Reason. If the Executive's employment with the Company is terminated by the Company (other than for Cause, Disability or Death) or by the Executive for Good Reason within 24 months following the Change in Control Date, then the Executive shall be entitled to the following benefits:

(i) the Company shall pay to the Executive in a lump sum in cash within 30 days after the Date of Termination the aggregate of the following amounts:

(1) the sum of (A) the Executive's base salary through the Date of Termination, (B) the annual bonus paid or payable (including any bonus or portion thereof which has been earned but deferred) for the most recently

completed fiscal year (if such bonus has not yet been paid), (C) the product of (x) the greater of (I) the annual bonus paid or payable to the Executive (including any bonus or portion thereof which has been earned but deferred) for the most recently completed fiscal year and (II) the Executive's target or reference bonus for the fiscal year in which the Date of Termination took place and (y) a fraction, the numerator of which is the number of days in the current fiscal year through the Date of Termination, and the denominator of which is 365 and (D) the amount of any compensation previously deferred by the Executive (together with any accrued interest or earnings thereon) and any accrued vacation pay, in each case to the extent not previously paid (the sum of the amounts described in clauses (A), (B), (C) and (D) shall be hereinafter referred to as the "Accrued Obligations"); and

(2) the amount equal to (A) three multiplied by (b) the sum of (x) the Executive's highest annual base salary in any twelve-month period (on a rolling basis) during the five-year period prior to the Change in Control Date and (y) the greater of (I) the Executive's highest annual bonus in any twelve-month period (on a rolling basis) during the five-year period prior to the Change in Control Date and (II) the Executive's target or reference bonus for the fiscal year in which the Change in Control took place.

(ii) for three years after the Date of Termination, or such longer period as may be provided by the terms of the appropriate plan, program, practice or policy, the Company shall continue to provide benefits (including, without limitation, automobile, retirement, medical, dental, life insurance and disability benefits) to the Executive and the Executive's family at least equal to those which would have been provided to them if the Executive's employment had not been terminated, in accordance with the applicable benefit plans in effect on the Measurement Date or, if more favorable to the Executive and the Executive's family, in effect generally at any time thereafter with respect to other peer executives of the Company and its affiliated companies; provided, however, that if the Executive becomes reemployed with another employer and is eligible to receive a particular type of benefits (e.g., medical benefits) from such employer on terms at least as favorable to the Executive and the Executive's family as those being provided by the Company, then the Company shall no longer be required to provide those particular benefits to the Executive and the Executive's family; and provided further, however, that (A) if any particular benefits cannot be provided because of plan or regulatory restrictions, then the Company will pay to the Executive an amount equal to the cost the Executive will incur in acquiring such benefits directly as a result of the Company not providing such benefits and (B) to the extent the Company determines that the Executive's qualifying event for purposes of continuation of medical benefits under COBRA occurs on the Executive's Date of Termination, such period of continuation of benefits shall not be counted against or otherwise reduce the period for which the Company must provide continuation of medical benefits under this Section 4.2(a)(ii) unless the Executive otherwise agrees;

(iii) to the extent not previously paid or provided, the Company shall timely pay or provide to the Executive any other amounts or benefits required to be paid or provided or which the Executive is eligible to receive following the Executive's termination of employment under any plan, program, policy, practice, contract or agreement of the Company and its affiliated companies (such other amounts and benefits shall be hereinafter referred to as the "Other Benefits"); and

(iv) Retirement Plan Benefits. If not already vested, the Executive shall be deemed fully vested as of the Measurement Date in any Company retirement plans or other written agreements between the Executive and the Company relating to pay or other benefits upon retirement in which the Executive was a participant, party or beneficiary immediately prior to the Change in Control, and any additional plans or agreements in which such Executive became a participant, party or beneficiary after the Change in Control and before the Date of Termination. In addition to the foregoing, for purposes of determining the amounts to be paid to the Executive under such plans or agreements, the years of service with the Company and the age of the Executive under all such plans and agreements shall be deemed increased by thirty-six (36) months. For purposes of this Section 4.2 (a)(iv), the term "plans" includes, without limitation, the Company's qualified pension plan, non-qualified pension plans, profit-sharing plans and 401(k) plans, and any companion, successor or amended plans, and the term "agreements" encompasses, without limitation, the terms of any offer letter leading to the Executive's employment with the Company where the Executive was a signatory thereto, any written amendments to the foregoing and any subsequent amendments on such matters. In the event the terms of the plans referenced in this Section 4.2 (a)(iv) do not for any reason coincide with the provisions of this Section 4.2 (a)(iv) (e.g., if plan amendments would cause disqualification of qualified plans), the Executive shall be entitled to receive from the Company, under the terms of this Agreement, an amount equal to all amounts the Executive would have received , at the time the Executive would have received such amounts, had all such plans continued in existence as in effect on the date of this Agreement after being amended to coincide with the terms of this Section 4.2 (a)(iv).

(b) Resignation without Good Reason; Termination for Death or Disability. If the Executive voluntarily terminates his or her employment with the Company within 24 months following the Change in Control Date, excluding a termination for Good Reason, or if the Executive's employment with the Company is terminated by reason of the Executive's death or Disability within 24 months following the Change in Control Date, then the Company shall (i) pay the Executive (or the Executive's estate, if applicable), in a lump sum in cash within 30 days after the Date of Termination, the Accrued Obligations and (ii) timely pay or provide to the Executive the Other Benefits.

(c) Termination for Cause. If the Company terminates the Executive's employment with the Company for Cause within 24 months following the Change in Control Date, then the Company shall (i) pay the Executive, in a lump sum in cash within 30 days after the Date of Termination, the sum of (A) the Executive's annual base salary through the Date of Termination and (B) the amount of any compensation previously deferred by the Executive, in each case to the extent not previously paid, and (ii) timely pay or provide to the Executive the Other Benefits.

4.3 Taxes.

(a) In the event that the Company undergoes a "Change in Ownership or Control" (as defined below), and thereafter, the Executive becomes eligible to receive "Contingent Compensation Payments" (as defined below) the Company shall, as soon as administratively feasible after the Executive becomes so eligible determine and notify the Executive (with reasonable detail regarding the basis for its determinations) (i) which of the payments or benefits due to the Executive following such Change in Ownership or Control constitute Contingent Compensation Payments, (ii) the amount, if any, of the excise tax (the "Excise Tax") payable pursuant to Section 4999 of the Internal Revenue Code of 1986, as amended (the "Code"), by the Executive with respect to such Contingent Compensation Payment and (iii) the amount of the "Gross-Up Payment" (as defined below) due to the Executive with respect to such Contingent Compensation Payment. Within 30 days after delivery of such notice to the Executive, the Executive shall deliver a response to the Company (the "Executive Response") stating either (A) that the Executive agrees with the Company's determination pursuant to the preceding sentence or (B) that the Executive disagrees with such determination, in which case the Executive shall indicate which payment and/or benefits should be characterized as a Contingent Compensation Payment, the amount of the Excise Tax with respect to such Contingent Compensation Payment and the amount of the Gross-Up Payment due to the Executive with respect to such Contingent Compensation Payment. If the Executive states in the Executive Response that the Executive agrees with the Company's determination, the Company shall make the Gross-Up Payment to the Executive within three business days following delivery to the Company of the Executive Response. If the Executive states in the Executive Response that the Executive disagrees with the Company's determination, then, for a period of 15 days following delivery of the Executive Response, the Executive and the Company shall use good faith efforts to resolve such dispute. If such dispute is not resolved within such 15-day period, such dispute shall be settled exclusively by arbitration in Boston, Massachusetts, in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction. The Company shall, within three business days following delivery to the Company of the Executive Response, make to the Executive those Gross-Up Payments as to which there is no dispute between the Company and the Executive regarding whether they should be made. The balance of the Gross-Up Payments shall be made within three business days following the resolution of such dispute. The amount of any payments to be made to the Executive following the resolution of such dispute shall be increased by the amount of the accrued interest thereon computed at the prime rate announced from time to time by The Wall Street Journal compounded monthly from the date that such payments originally were due. In the event that the Executive fails to deliver an Executive Response on or before the required date, the Company's initial determination shall be final. The Gross-Up Payment shall be made no later than the end of the Executive's taxable year next following the Executive's taxable year in which he paid the taxes related to the Gross-Up Payment.

(b) For purposes of this Section 4.3, the following terms shall have the following respective meanings:

(i) "Change in Ownership or Control" shall mean a change in the ownership or effective control of the Company or in the ownership of a substantial portion of the assets of the Company determined in accordance with Section 280G(b)(2) of the Code.

(ii) "Contingent Compensation Payment" shall mean any payment (or benefit) in the nature of compensation that is made or supplied to a "disqualified individual" (as defined in Section 280G(c) of the Code) and that is contingent (within the meaning of Section 280G(b)(2)(A)(i) of the Code) on a Change in Ownership or Control of the Company.

(iii) "Gross-Up Payment" shall mean an amount equal to the sum of (i) the amount of the Excise Tax payable with respect to a Contingent Compensation Payment and (ii) the amount necessary to pay all additional taxes imposed on (or economically borne by) the Executive (including the Excise Taxes, state and federal income taxes and all applicable withholding taxes) attributable to the receipt of such Gross-Up Payment. For purposes of the preceding sentence, all taxes attributable to the receipt of the Gross-Up Payment shall be computed assuming the application of the maximum tax rates provided by law.

4.4 Outplacement Services. In the event the Executive is terminated by the Company (other than for Cause, Disability or Death), or the Executive terminates employment for Good Reason, within 24 months following the Change in Control Date, the Company shall provide outplacement services through one or more outside firms of the Executive's choosing up to an aggregate of $25,000 with such services to extend until the earlier of (i) 12 months following the termination of Executive's employment or (ii) the date the Executive secures full time employment.

4.5 Mitigation. The Executive shall not be required to mitigate the amount of any payment or benefits provided for in this Section 4 by seeking other employment or otherwise. Further, except as provided in Section 4.2(a)(ii), the amount of any payment or benefits provided for in this Section 4 shall not be reduced by any compensation earned by the Executive as a result of employment by another employer, by retirement benefits, by offset against any amount claimed to be owed by the Executive to the Company or otherwise.

4.6 Payments Subject to Section 409A. Subject to the provisions in this Section 4.6, any severance payments or benefits under this Agreement shall begin only upon the date of the Employee's "separation from service" (determined as set forth below) which occurs on or after the date of termination of the Employee's employment. The following rules shall apply with respect to distribution of the payments and benefits, if any, to be provided to the Employee under this Agreement:

(a) It is intended that each installment of the severance payments and benefits provided under this Agreement shall be treated as a separate "payment" for purposes of Section 409A of the Code and the guidance issued thereunder ("Section 409A"). Neither the Company nor the Employee shall have the right to accelerate or defer the delivery of any such payments or benefits except to the extent specifically permitted or required by Section 409A.

(b) If, as of the date of Employee's "separation from service" from the Company, the Employee is not a "specified employee" (within the meaning of Section 409A), then each installment of the severance payments and benefits shall be made on the dates and terms set forth in this Agreement.

(c) If, as of the date of the Employee's "separation from service" from the Company, the Employee is a "specified employee" (within the meaning of Section 409A), then:

(i) Each installment of the severance payments and benefits due under this Agreement that, in accordance with the dates and terms set forth herein, will in all circumstances, regardless of when the separation from service occurs, be paid within the Short-Term Deferral Period (as hereinafter defined) shall be treated as a short-term deferral within the meaning of Treasury Regulation § 1.409A-1(b)(4) to the maximum extent permissible under Section 409A. For purposes of this Agreement, the "Short-Term Deferral Period" means the period ending on the later of the fifteenth day of the third month following the end of the Employee's tax year in which the separation from service occurs and the fifteenth day of the third month following the end of the Company's tax year in which the separation from service occurs; and

(ii) Each installment of the severance payments and benefits due under this Agreement that is not described in subsection (c)(i) above and that would, absent this subsection, be paid within the six-month period following the Employee's "separation from service" from the Company shall not be paid until the date that is six months and one day after such separation from service (or, if earlier, the Employee's death), with any such installments that are required to be delayed being accumulated during the six-month period and paid in a lump sum on the date that is six months and one day following the Employee's separation from service and any subsequent installments, if any, being paid in accordance with the dates and terms set forth herein; provided, however, that the preceding provisions of this sentence shall not apply to any installment of severance payments and benefits if and to the maximum extent that such installment is deemed to be paid under a separation pay plan that does not provide for a deferral of compensation by reason of the application of Treasury Regulation § 1.409A-1(b)(9)(iii) (relating to separation pay upon an involuntary separation from service). Any installments that qualify for the exception under Treasury Regulation § 1.409A-1(b)(9)(iii) must be paid no later than the last day of the Employee's second taxable year following the taxable year in which the separation from service occurs.

(d) The determination of whether and when the Employee's separation from service from the Company has occurred shall be made and in a manner consistent with, and based on the presumptions set forth in, Treasury Regulation § 1.409A-1(h). Solely for purposes of this paragraph (d), "Company" shall include all persons with whom the Company would be considered a single employer under Section 414(b) and 414(c) of the Code.

(e) All reimbursements and in-kind benefits provided under this Agreement shall be made or provided in accordance with the requirements of Section 409A to the extent that such reimbursements or in-kind benefits are subject to Section 409A, including, where applicable, the requirements that (i) any reimbursement is for expenses incurred during the Employee's lifetime (or during a shorter period of time specified in this Agreement), (ii) the amount of expenses eligible for reimbursement during a calendar year may not affect the expenses eligible for reimbursement in any other calendar year, (iii) the reimbursement of an eligible expense will be made on or before the last day of the calendar year following the year in which the expense is incurred and (iv) the right to reimbursement is not subject to set off or liquidation or exchange for any other benefit.

(f) This Agreement is intended to comply with the provisions of Section 409A and the Agreement shall, to the extent practicable, be construed in accordance therewith. The Company makes no representation or warranty and shall have no liability to the Executive or any other person if any provisions of this Agreement are determined to constitute deferred compensation subject to Section 409A and do not satisfy an exemption from, or the conditions of, Section 409A.

5. <u>Disputes</u>.

5.1 <u>Settlement of Disputes; Arbitration</u>. All claims by the Executive for benefits under this Agreement shall be directed to and determined by the Board of Directors of the Company and shall be in writing. Any denial by the Board of Directors of a claim for benefits under this Agreement shall be delivered to the Executive in writing and shall set forth the specific reasons for the denial and the specific provisions of this Agreement relied upon. The Board of Directors shall afford a reasonable opportunity to the Executive for a review of the decision denying a claim. Any further dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration in Boston, Massachusetts, in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction.

5.2 <u>Expenses</u>. The Company agrees to pay as incurred, to the full extent permitted by law, all legal, accounting and other fees and expenses which the Executive may reasonably incur as a result of any claim or contest (regardless of the outcome thereof) by the Company, the Executive or others regarding the validity or enforceability of, or liability under, any provision of this Agreement or any guarantee of performance thereof (including as a result of any contest by the Executive regarding the amount of any payment or benefits pursuant to this Agreement), plus in each case interest on any delayed payment at the applicable Federal rate provided for in Section 7872(f)(2)(A) of the Code.

6. Successors.

6.1 Successor to Company. The Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business or assets of the Company expressly to assume and agree to perform this Agreement to the same extent that the Company would be required to perform it if no such succession had taken place. Failure of the Company to obtain an assumption of this Agreement at or prior to the effectiveness of any succession shall be a breach of this Agreement and shall constitute Good Reason if the Executive elects to terminate employment, except that for purposes of implementing the foregoing, the date on which any such succession becomes effective shall be deemed the Date of Termination. As used in this Agreement, "Company" shall mean the Company as defined above and any successor to its business or assets as aforesaid which assumes and agrees to perform this Agreement, by operation of law or otherwise.

6.2 Successor to Executive. This Agreement shall inure to the benefit of and be enforceable by the Executive's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees and legatees. If the Executive should die while any amount would still be payable to the Executive or the Executive's family hereunder if the Executive had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to the executors, personal representatives or administrators of the Executive's estate.

7. Notice. All notices, instructions and other communications given hereunder or in connection herewith shall be in writing. Any such notice, instruction or communication shall be sent either (i) by registered or certified mail, return receipt requested, postage prepaid, or (ii) prepaid via a reputable nationwide overnight courier service, in each case addressed to the Company, at One Technology Park Drive, Westford, Massachusetts 01886 and to the Executive at the Executive's principal residence as currently reflected on the Company's records (or to such other address as either the Company or the Executive may have furnished to the other in writing in accordance herewith). Any such notice, instruction or communication shall be deemed to have been delivered five business days after it is sent by registered or certified mail, return receipt requested, postage prepaid, or one business day after it is sent via a reputable nationwide overnight courier service. Either party may give any notice, instruction or other communication hereunder using any other means, but no such notice, instruction or other communication shall be deemed to have been duly delivered unless and until it actually is received by the party for whom it is intended.

8. Miscellaneous.

8.1 Severability. The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement, which shall remain in full force and effect.

8.2 Injunctive Relief. The Company and the Executive agree that any breach of this Agreement by the Company is likely to cause the Executive substantial and irrevocable damage and therefore, in the event of any such breach, in addition to such other remedies which may be available, the Executive shall have the right to specific performance and injunctive relief.

8.3 Governing Law. The validity, interpretation, construction and performance of this Agreement shall be governed by the internal laws of the Commonwealth of Massachusetts, without regard to conflicts of law principles.

8.4 Waivers. No waiver by the Executive at any time of any breach of, or compliance with, any provision of this Agreement to be performed by the Company shall be deemed a waiver of that or any other provision at any subsequent time.

8.5 Counterparts. This Agreement may be executed in counterparts, each of which shall be deemed to be an original but both of which together shall constitute one and the same instrument.

8.6 Tax Withholding. Any payments provided for hereunder shall be paid net of any applicable tax withholding required under federal, state or local law.

8.7 Entire Agreement. This Agreement sets forth the entire agreement of the parties hereto in respect of the subject matter contained herein and supersedes all prior agreements, promises, covenants, arrangements, communications, representations or warranties, whether oral or written, by any officer, employee or representative of any party hereto in respect of the subject matter contained herein; and any prior agreement of the parties hereto in respect of the subject matter contained herein is hereby terminated and cancelled.

8.8 Amendments. This Agreement may be amended or modified only by a written instrument executed by both the Company and the Executive.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first set forth above.

KĀDANT INC.

/s/ Thomas M. O'Brien

By: Thomas M. O'Brien
Executive Vice President and Chief Financial Officer

EXECUTIVE

/s/ William A. Rainville

William A. Rainville

<u>FORM OF</u>

<u>AMENDED AND RESTATED EXECUTIVE RETENTION AGREEMENT</u>

THIS AMENDED AND RESTATED EXECUTIVE RETENTION AGREEMENT by and between KĀDANT INC., a Delaware corporation (the "Company"), and [Name] (the "Executive") is made as of December 9, 2008 (the "Effective Date").

WHEREAS, the Company and the Executive are parties to that certain Executive Retention Agreement dated as of August 8, 2001, as amended and restated effective as of December 5, 2006 (the "Original Agreement");

WHEREAS, the Board of Directors of the Company (the "Board") recognizes that, as is the case with many publicly-held corporations, the possibility of a change in control of the Company exists and that such possibility, and the uncertainty and questions which it may raise among key personnel, may result in the departure or distraction of key personnel to the detriment of the Company and its stockholders;

WHEREAS, the Board has determined that appropriate steps should be taken to reinforce and encourage the continued employment and dedication of the Company's key personnel without distraction from the possibility of a change in control of the Company and related events and circumstances; and

WHEREAS, the Board and the Executive intend that the Original Agreement comply with the provisions of Section 409A of the Internal Revenue Code (the "Code") and for that purpose desire to amend and restate the Original Agreement; and

NOW, THEREFORE, as an inducement for and in consideration of the Executive remaining in the Company's employ, the Executive and the Company agree as follows:

1. <u>Key Definitions</u>.

As used herein, the following terms shall have the following respective meanings:

1.1 "<u>Change in Control</u>" means an event or occurrence set forth in any one or more of subsections (a) through (d) below (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) (a "Person") of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 20% or more of either (i) the then-outstanding shares of common stock of the Company (the "Outstanding Company Common Stock") or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this Section 1.1; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the Board of Directors of a successor corporation to the Company), where the term "Continuing Director" means at any date a member of the Board (i) who was a member of the Board on the date of the execution of this Agreement or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a "Business Combination"), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Company Common Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 80% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company's assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the "Acquiring Corporation") in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Company Common Stock and Outstanding Company Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 20% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

1.2 "Change in Control Date" means the first date during the Term (as defined in Section 2) on which a Change in Control occurs. Anything in this Agreement to the contrary notwithstanding, if (a) a Change in Control occurs, (b) the Executive's employment with the Company is terminated prior to the date on which the Change in Control occurs, and (c) it is reasonably demonstrated by the Executive that such termination of employment (i) was at the request of a third party who has taken steps reasonably calculated to effect a Change in Control or (ii) otherwise arose in connection with or in anticipation of a Change in Control, then for all purposes of this Agreement the "Change in Control Date" shall mean the date immediately prior to the date of such termination of employment.

1.3 "Cause" means the Executive's willful engagement in illegal conduct or gross misconduct after the Change in Control Date which is materially and demonstrably injurious to the Company. For purposes of this Section 1.3, no act or failure to act by the Executive shall be considered "willful" unless it is done, or omitted to be done, in bad faith and without reasonable belief that the Executive's action or omission was in the best interests of the Company.

1.4 "Good Reason" means the occurrence, without the Executive's written consent, of any of the events or circumstances set forth in clauses (a) through (g) below on or after the Change in Control Date. Notwithstanding the occurrence of any such event or circumstance, such occurrence shall not be deemed to constitute Good Reason if, prior to the Date of Termination specified in the Notice of Termination (each as defined in Section 3.2(a)) given by the Executive in respect thereof, such event or circumstance has been fully corrected within 30 days after notice thereof and the Executive has been reasonably compensated for any losses or damages resulting therefrom.

(a) the assignment to the Executive of duties inconsistent in any material respect with the Executive's position (including status, offices, titles and reporting requirements, including but not limited to a change in any of the foregoing that results in the Executive no longer being an officer of a public company), authority or responsibilities in effect immediately prior to the earliest to occur of (i) the Change in Control Date, (ii) the date of the execution by the Company of the initial written agreement or instrument providing for the Change in Control or (iii) the date of the adoption by the Board of Directors of a resolution providing for the Change in Control (with the earliest to occur of such dates referred to herein as the "Measurement Date") or a material diminution in such position, authority or responsibilities;

(b) a reduction in the Executive's annual base salary as in effect on the Measurement Date or as the same was or may be increased thereafter from time to time;

(c) the failure by the Company to (i) continue in effect any material compensation or benefit plan or program (including without limitation any life insurance, medical, health and accident or disability plan and any vacation or automobile program or policy) (a "Benefit Plan") in which the Executive participates or which is applicable to the Executive immediately prior to the Measurement Date, unless an equitable arrangement (embodied in an ongoing substitute or alternative plan) has been made with respect to such plan or program, (ii) continue the Executive's participation therein (or in such substitute or alternative plan) on a basis not materially less favorable than the basis existing immediately prior to the Measurement Date (iii) award cash bonuses to the Executive in amounts and in a manner substantially consistent with past practice in light of the Company's financial performance or (iv) continue to provide any material fringe benefit enjoyed by Executive immediately prior to the Measurement Date;

(d) a change by the Company in the location at which the Executive performs his or her principal duties for the Company to a new location that is both (i) outside a radius of 50 miles from the Executive's principal residence immediately prior to the Measurement Date and (ii) more than 30 miles from the location at which the Executive performed his or her principal duties for the Company immediately prior to the Measurement Date; or a requirement by the Company that the Executive travel on Company business to a substantially greater extent than required immediately prior to the Measurement Date;

(e) the failure of the Company to obtain the agreement from any successor to the Company to assume and agree to perform this Agreement, as required by Section 6.1;

(f) a material breach of this Agreement; or

(g) any failure of the Company to pay or provide to the Executive any portion of the Executive's compensation or benefits due under any Benefit Plan within seven days of the date such compensation or benefits are due, or any material breach by the Company of this Agreement or any employment agreement with the Executive.

The Executive's right to terminate his or her employment for Good Reason shall not be affected by the Executive's incapacity due to physical or mental illness.

1.5 "Disability" means the Executive's absence from the full-time performance of the Executive's duties with the Company for 180 consecutive calendar days as a result of incapacity due to mental or physical illness which is determined to be total and permanent by a physician selected by the Company or its insurers and acceptable to the Executive or the Executive's legal representative.

2. Term of Agreement. This Agreement, and all rights and obligations of the parties hereunder, shall take effect upon the Effective Date and shall expire upon the first to occur of (a) the expiration of the Term (as defined below) if a Change in Control has not occurred during the Term, (b) the date 24 months after the Change in Control Date, if the Executive is still employed by the Company as of such later date, or (c) the fulfillment by the Company of all of its obligations under Sections 4 and 5.2 if the Executive's employment with the Company terminates within 24 months following the Change in Control Date. "Term" shall mean the period commencing as of the Effective Date and continuing in effect through December 31, 2011; provided, however, that commencing on January 1, 2012 and each January 1, thereafter, the Term shall be automatically extended for one additional year unless, not later than 90 days prior to the scheduled expiration of the Term (or any extension thereof), the Company shall have given the Executive written notice that the Term will not be extended.

3. Employment Status; Termination Following Change in Control.

3.1 Not an Employment Contract. The Executive acknowledges that this Agreement does not constitute a contract of employment or impose on the Company any obligation to retain the Executive as an employee and that this Agreement does not prevent the Executive from terminating employment at any time. If the Executive's employment with the Company terminates for any reason and subsequently a Change in Control shall occur, the Executive shall not be entitled to any benefits hereunder except as otherwise provided pursuant to Section 1.2.

3.2 Termination of Employment.

(a) If the Change in Control Date occurs during the Term, any termination of the Executive's employment by the Company or by the Executive within 24 months following the Change in Control Date (other than due to the death of the Executive) shall be communicated by a written notice to the other party hereto (the "Notice of Termination"), given in accordance with Section 7. Any Notice of Termination shall: (i) indicate the specific termination provision (if any) of this Agreement relied upon by the party giving such notice, (ii) to the extent applicable, set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of the Executive's employment under the provision so indicated and (iii) specify the Date of Termination (as defined below). The effective date of an employment termination (the "Date of Termination") shall be the close of business on the date specified in the Notice of Termination (which date may not be less than 15 days or more than 120 days after the date of delivery of such Notice of Termination), in the case of a termination other than one due to the Executive's death, or the date of the Executive's death, as the case may be. In the event the Company fails to satisfy the requirements of Section 3.2(a) regarding a Notice of Termination, the purported termination of the Executive's employment pursuant to such Notice of Termination shall not be effective for purposes of this Agreement.

(b) The failure by the Executive or the Company to set forth in the Notice of Termination any fact or circumstance which contributes to a showing of Good Reason or Cause shall not waive any right of the Executive or the Company, respectively, hereunder or preclude the Executive or the Company, respectively, from asserting any such fact or circumstance in enforcing the Executive's or the Company's rights hereunder.

(c) Any Notice of Termination for Cause given by the Company must be given within 90 days of the occurrence of the event(s) or circumstance(s) that constitute(s) Cause. Prior to any Notice of Termination for Cause being given (and prior to any termination for Cause being effective), the Executive shall be entitled to a hearing before the Board of Directors of the Company at which the Executive may, at the Executive's election, be represented by counsel and at which the Executive shall have a reasonable opportunity to be heard. Such hearing shall be held on not less than 15 days prior written notice to the Executive stating the Board of Directors' intention to terminate the Executive for Cause and stating in detail the particular event(s) or circumstance(s) that the Board of Directors believes constitutes Cause for termination.

(d) Any Notice of Termination for Good Reason given by the Executive must be given within 90 days of the first occurrence of the event(s) or circumstance(s) that constitute(s) Good Reason.

4. <u>Benefits to Executive</u>.

4.1 <u>Stock Acceleration</u>. If the Change in Control Date occurs during the Term, then, effective upon the Change in Control Date, (a) each outstanding option to purchase shares of Common Stock of the Company held by the Executive shall become immediately exercisable in full and will no longer be subject to a right of repurchase by the Company and (b) each outstanding restricted stock award shall be deemed to be fully vested and will no longer be subject to a right of repurchase by the Company.

4.2 <u>Compensation</u>. If the Change in Control Date occurs during the Term and the Executive's employment with the Company terminates within 24 months following the Change in Control Date, the Executive shall be entitled to the following benefits:

(a) <u>Termination Without Cause or for Good Reason</u>. If the Executive's employment with the Company is terminated by the Company (other than for Cause, Disability or Death) or by the Executive for Good Reason within 24 months following the Change in Control Date, then the Executive shall be entitled to the following benefits:

(i) the Company shall pay to the Executive in a lump sum in cash within 30 days after the Date of Termination the aggregate of the following amounts:

(1) the sum of (A) the Executive's base salary through the Date of Termination, (B) the annual bonus paid or payable (including any bonus or portion thereof which has been earned but deferred) for the most recently completed fiscal year (if such bonus has not yet been paid), (C) the product of (x) the greater of (I) the annual bonus paid or payable to the Executive (including any bonus or portion thereof which has been earned but deferred) for the most recently completed fiscal year and (II) the Executive's target or reference bonus for the fiscal year in which the Date of Termination took place and (y) a fraction, the numerator of which is the number of days in the current fiscal year through the Date of Termination, and the denominator of which is 365 and (D) the amount of any compensation previously deferred by the Executive (together with any accrued interest or earnings thereon) and any accrued vacation pay, in each case to the extent not previously paid (the sum of the amounts described in clauses (A), (B), (C) and (D) shall be hereinafter referred to as the "Accrued Obligations"); and

(2) the amount equal to (A) two multiplied by (b) the sum of (x) the Executive's highest annual base salary in any twelve-month period (on a rolling basis) during the five-year period prior to the Change in Control Date and (y) the greater of (I) the Executive's highest annual bonus in any twelve-month period (on a rolling basis) during the five-year period prior to the Change in Control Date and (II) the Executive's target or reference bonus for the fiscal year in which the Change in Control took place.

(ii) for two years after the Date of Termination, or such longer period as may be provided by the terms of the appropriate plan, program, practice or policy, the Company shall continue to provide benefits (including, without limitation, automobile, retirement, medical, dental, life insurance and disability benefits) to the Executive and the Executive's family at least equal to those which would have been provided to them if the Executive's employment had not been terminated, in accordance with the applicable benefit plans in effect on the Measurement Date or, if more favorable to the Executive and the Executive's family, in effect generally at any time thereafter with respect to other peer executives of the Company and its affiliated companies; provided, however, that if the Executive becomes reemployed with another employer and is eligible to receive a particular type of benefits (e.g., medical benefits) from such employer on terms at least as favorable to the Executive and the Executive's family as those being provided by the Company, then the Company shall no longer be required to provide those particular benefits to the Executive and the Executive's family; and provided further, however, that (A) if any particular benefits cannot be provided because of plan or regulatory restrictions, then the Company will pay to the Executive an amount equal to the cost the Executive will incur in acquiring such benefits directly as a result of the Company not providing such benefits and (B) to the extent the Company determines that the Executive's qualifying event for purposes of continuation of medical benefits under COBRA occurs on the Executive's Date of Termination, such period of continuation of benefits shall not be counted against or otherwise reduce the period for which the Company must provide continuation of medical benefits under this Section 4.2(a)(ii) unless the Executive otherwise agrees;

(iii) to the extent not previously paid or provided, the Company shall timely pay or provide to the Executive any other amounts or benefits required to be paid or provided or which the Executive is eligible to receive following the Executive's termination of employment under any plan, program, policy, practice, contract or agreement of the Company and its affiliated companies (such other amounts and benefits shall be hereinafter referred to as the "Other Benefits"); and

(iv) Retirement Plan Benefits. If not already vested, the Executive shall be deemed fully vested as of the Measurement Date in any Company retirement plans or other written agreements between the Executive and the Company relating to pay or other benefits upon retirement in which the Executive was a participant, party or beneficiary immediately prior to the Change in Control, and any additional plans or agreements in which such Executive became a participant, party or beneficiary after the Change in Control and before the Date of Termination. In addition to the foregoing, for purposes of determining the amounts to be paid to the Executive under such plans or agreements, the years of service with the Company and the age of the Executive under all such plans and agreements shall be deemed increased by twenty-four (24) months. For purposes of this Section 4.2 (a)(iv), the term "plans" includes, without limitation, the Company's qualified pension plan, non-qualified pension plans, profit-sharing plans and 401(k) plans, and any companion, successor or amended plans, and the term "agreements" encompasses, without limitation, the terms of any offer letter leading to the Executive's employment with the Company where the Executive was a signatory thereto, any written amendments to the foregoing and any subsequent amendments on such matters. In the event the terms of the plans referenced in this Section 4.2 (a)(iv) do not for any reason coincide with the provisions of this Section 4.2 (a)(iv) (e.g., if plan amendments would cause disqualification of qualified plans), the Executive shall be entitled to receive from the Company, under the terms of this Agreement, an amount equal to all amounts the Executive would have received , at the time the Executive would have received such amounts, had all such plans continued in existence as in effect on the date of this Agreement after being amended to coincide with the terms of this Section 4.2 (a)(iv).

(b) Resignation without Good Reason; Termination for Death or Disability. If the Executive voluntarily terminates his or her employment with the Company within 24 months following the Change in Control Date, excluding a termination for Good Reason, or if the Executive's employment with the Company is terminated by reason of the Executive's death or Disability within 24 months following the Change in Control Date, then the Company shall (i) pay the Executive (or the Executive's estate, if applicable), in a lump sum in cash within 30 days after the Date of Termination, the Accrued Obligations and (ii) timely pay or provide to the Executive the Other Benefits.

(c) Termination for Cause. If the Company terminates the Executive's employment with the Company for Cause within 24 months following the Change in Control Date, then the Company shall (i) pay the Executive, in a lump sum in cash within 30 days after the Date of Termination, the sum of (A) the Executive's annual base salary through the Date of Termination and (B) the amount of any compensation previously deferred by the Executive, in each case to the extent not previously paid, and (ii) timely pay or provide to the Executive the Other Benefits.

4.3 Taxes.

(a) In the event that the Company undergoes a "Change in Ownership or Control" (as defined below), and thereafter, the Executive becomes eligible to receive "Contingent Compensation Payments" (as defined below) the Company shall, as soon as administratively feasible after the Executive becomes so eligible determine and notify the Executive (with reasonable detail regarding the basis for its determinations) (i) which of the payments or benefits due to the Executive following such Change in Ownership or Control constitute Contingent Compensation Payments, (ii) the amount, if any, of the excise tax (the "Excise Tax") payable pursuant to Section 4999 of the Internal Revenue Code of 1986, as amended (the "Code"), by the Executive with respect to such Contingent Compensation Payment and (iii) the amount of the "Gross-Up Payment" (as defined below) due to the Executive with respect to such Contingent Compensation Payment. Within 30 days after delivery of such notice to the Executive, the Executive shall deliver a response to the Company (the "Executive Response") stating either (A) that the Executive agrees with the Company's determination pursuant to the preceding sentence or (B) that the Executive disagrees with such determination, in which case the Executive shall indicate which payment and/or benefits should be characterized as a Contingent Compensation Payment, the amount of the Excise Tax with respect to such Contingent Compensation Payment and the amount of the Gross-Up Payment due to the Executive with respect to such Contingent Compensation Payment. If the Executive states in the Executive Response that the Executive agrees with the Company's determination, the Company shall make the Gross-Up Payment to the Executive within three business days following delivery to the Company of the Executive Response. If the Executive states in the Executive Response that the Executive disagrees with the Company's determination, then, for a period of 15 days following delivery of the Executive Response, the Executive and the Company shall use good faith efforts to resolve such dispute. If such dispute is not resolved within such 15-day period, such dispute shall be settled exclusively by arbitration in Boston, Massachusetts, in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction. The Company shall, within three business days following delivery to the Company of the Executive Response, make to the Executive those Gross-Up Payments as to which there is no dispute between the Company and the Executive regarding whether they should be made. The balance of the Gross-Up Payments shall be made within three business days following the resolution of such dispute. The amount of any payments to be made to the Executive following the resolution of such dispute shall be increased by the amount of the accrued interest thereon computed at the prime rate announced from time to time by The Wall Street Journal compounded monthly from the date that such payments originally were due. In the event that the Executive fails to deliver an Executive Response on or before the required date, the Company's initial determination shall be final. The Gross-Up Payment shall be made no later than the end of the Executive's taxable year next following the Executive's taxable year in which he paid the taxes related to the Gross-Up Payment.

(b) For purposes of this Section 4.3, the following terms shall have the following respective meanings:

(i) "Change in Ownership or Control" shall mean a change in the ownership or effective control of the Company or in the ownership of a substantial portion of the assets of the Company determined in accordance with Section 280G(b)(2) of the Code.

(ii) "Contingent Compensation Payment" shall mean any payment (or benefit) in the nature of compensation that is made or supplied to a "disqualified individual" (as defined in Section 280G(c) of the Code) and that is contingent (within the meaning of Section 280G(b)(2)(A)(i) of the Code) on a Change in Ownership or Control of the Company.

(iii) "Gross-Up Payment" shall mean an amount equal to the sum of (i) the amount of the Excise Tax payable with respect to a Contingent Compensation Payment and (ii) the amount necessary to pay all additional taxes imposed on (or economically borne by) the Executive (including the Excise Taxes, state and federal income taxes and all applicable withholding taxes) attributable to the receipt of such Gross-Up Payment. For purposes of the preceding sentence, all taxes attributable to the receipt of the Gross-Up Payment shall be computed assuming the application of the maximum tax rates provided by law.

4.4 Outplacement Services. In the event the Executive is terminated by the Company (other than for Cause, Disability or Death), or the Executive terminates employment for Good Reason, within 24 months following the Change in Control Date, the Company shall provide outplacement services through one or more outside firms of the Executive's choosing up to an aggregate of $20,000 with such services to extend until the earlier of (i) 12 months following the termination of Executive's employment or (ii) the date the Executive secures full time employment.

4.5 Mitigation. The Executive shall not be required to mitigate the amount of any payment or benefits provided for in this Section 4 by seeking other employment or otherwise. Further, except as provided in Section 4.2(a)(ii), the amount of any payment or benefits provided for in this Section 4 shall not be reduced by any compensation earned by the Executive as a result of employment by another employer, by retirement benefits, by offset against any amount claimed to be owed by the Executive to the Company or otherwise.

4.6 **Payments Subject to Section 409A.** Subject to the provisions in this Section 4.6, any severance payments or benefits under this Agreement shall begin only upon the date of the Employee's "separation from service" (determined as set forth below) which occurs on or after the date of termination of the Employee's employment. The following rules shall apply with respect to distribution of the payments and benefits, if any, to be provided to the Employee under this Agreement:

(a) It is intended that each installment of the severance payments and benefits provided under this Agreement shall be treated as a separate "payment" for purposes of Section 409A of the Code and the guidance issued thereunder ("Section 409A"). Neither the Company nor the Employee shall have the right to accelerate or defer the delivery of any such payments or benefits except to the extent specifically permitted or required by Section 409A.

(b) If, as of the date of Employee's "separation from service" from the Company, the Employee is not a "specified employee" (within the meaning of Section 409A), then each installment of the severance payments and benefits shall be made on the dates and terms set forth in this Agreement.

(c) If, as of the date of the Employee's "separation from service" from the Company, the Employee is a "specified employee" (within the meaning of Section 409A), then:

(i) Each installment of the severance payments and benefits due under this Agreement that, in accordance with the dates and terms set forth herein, will in all circumstances, regardless of when the separation from service occurs, be paid within the Short-Term Deferral Period (as hereinafter defined) shall be treated as a short-term deferral within the meaning of Treasury Regulation § 1.409A-1(b)(4) to the maximum extent permissible under Section 409A. For purposes of this Agreement, the "Short-Term Deferral Period" means the period ending on the later of the fifteenth day of the third month following the end of the Employee's tax year in which the separation from service occurs and the fifteenth day of the third month following the end of the Company's tax year in which the separation from service occurs; and

(ii) Each installment of the severance payments and benefits due under this Agreement that is not described in subsection (c)(i) above and that would, absent this subsection, be paid within the six-month period following the Employee's "separation from service" from the Company shall not be paid until the date that is six months and one day after such separation from service (or, if earlier, the Employee's death), with any such installments that are required to be delayed being accumulated during the six-month period and paid in a lump sum on the date that is six months and one day following the Employee's separation from service and any subsequent installments, if any, being paid in accordance with the dates and terms set forth herein; provided, however, that the preceding provisions of this sentence shall not apply to any installment of severance payments and benefits if and to the maximum extent that that such installment is deemed to be paid under a separation pay plan that does not provide for a deferral of compensation by reason of the application of Treasury Regulation § 1.409A-1(b)(9)(iii) (relating to separation pay upon an involuntary separation from service). Any installments that qualify for the exception under Treasury Regulation § 1.409A-1(b)(9)(iii) must be paid no later than the last day of the Employee's second taxable year following the taxable year in which the separation from service occurs.

(d) The determination of whether and when the Employee's separation from service from the Company has occurred shall be made and in a manner consistent with, and based on the presumptions set forth in, Treasury Regulation § 1.409A-1(h). Solely for purposes of this paragraph (d), "Company" shall include all persons with whom the Company would be considered a single employer under Section 414(b) and 414(c) of the Code.

(e) All reimbursements and in-kind benefits provided under this Agreement shall be made or provided in accordance with the requirements of Section 409A to the extent that such reimbursements or in-kind benefits are subject to Section 409A, including, where applicable, the requirements that (i) any reimbursement is for expenses incurred during the Employee's lifetime (or during a shorter period of time specified in this Agreement), (ii) the amount of expenses eligible for reimbursement during a calendar year may not affect the expenses eligible for reimbursement in any other calendar year, (iii) the reimbursement of an eligible expense will be made on or before the last day of the calendar year following the year in which the expense is incurred and (iv) the right to reimbursement is not subject to set off or liquidation or exchange for any other benefit.

(f) This Agreement is intended to comply with the provisions of Section 409A and the Agreement shall, to the extent practicable, be construed in accordance therewith. The Company makes no representation or warranty and shall have no liability to the Executive or any other person if any provisions of this Agreement are determined to constitute deferred compensation subject to Section 409A and do not satisfy an exemption from, or the conditions of, Section 409A.

5. Disputes.

5.1 Settlement of Disputes; Arbitration. All claims by the Executive for benefits under this Agreement shall be directed to and determined by the Board of Directors of the Company and shall be in writing. Any denial by the Board of Directors of a claim for benefits under this Agreement shall be delivered to the Executive in writing and shall set forth the specific reasons for the denial and the specific provisions of this Agreement relied upon. The Board of Directors shall afford a reasonable opportunity to the Executive for a review of the decision denying a claim. Any further dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration in Boston, Massachusetts, in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction.

5.2 Expenses. The Company agrees to pay as incurred, to the full extent permitted by law, all legal, accounting and other fees and expenses which the Executive may reasonably incur as a result of any claim or contest (regardless of the outcome thereof) by the Company, the Executive or others regarding the validity or enforceability of, or liability under, any provision of this Agreement or any guarantee of performance thereof (including as a result of any contest by the Executive regarding the amount of any payment or benefits pursuant to this Agreement), plus in each case interest on any delayed payment at the applicable Federal rate provided for in Section 7872(f)(2)(A) of the Code.

6. Successors.

6.1 Successor to Company. The Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business or assets of the Company expressly to assume and agree to perform this Agreement to the same extent that the Company would be required to perform it if no such succession had taken place. Failure of the Company to obtain an assumption of this Agreement at or prior to the effectiveness of any succession shall be a breach of this Agreement and shall constitute Good Reason if the Executive elects to terminate employment, except that for purposes of implementing the foregoing, the date on which any such succession becomes effective shall be deemed the Date of Termination. As used in this Agreement, “Company” shall mean the Company as defined above and any successor to its business or assets as aforesaid which assumes and agrees to perform this Agreement, by operation of law or otherwise.

6.2 Successor to Executive. This Agreement shall inure to the benefit of and be enforceable by the Executive’s personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees and legatees. If the Executive should die while any amount would still be payable to the Executive or the Executive’s family hereunder if the Executive had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to the executors, personal representatives or administrators of the Executive’s estate.

7. Notice. All notices, instructions and other communications given hereunder or in connection herewith shall be in writing. Any such notice, instruction or communication shall be sent either (i) by registered or certified mail, return receipt requested, postage prepaid, or (ii) prepaid via a reputable nationwide overnight courier service, in each case addressed to the Company, at One Technology Park Drive, Westford, Massachusetts 01886 and to the Executive at the Executive’s principal residence as currently reflected on the Company’s records (or to such other address as either the Company or the Executive may have furnished to the other in writing in accordance herewith). Any such notice, instruction or communication shall be deemed to have been delivered five business days after it is sent by registered or certified mail, return receipt requested, postage prepaid, or one business day after it is sent via a reputable nationwide overnight courier service. Either party may give any notice, instruction or other communication hereunder using any other means, but no such notice, instruction or other communication shall be deemed to have been duly delivered unless and until it actually is received by the party for whom it is intended.

8. Miscellaneous.

8.1 Severability. The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement, which shall remain in full force and effect.

8.2 Injunctive Relief. The Company and the Executive agree that any breach of this Agreement by the Company is likely to cause the Executive substantial and irrevocable damage and therefore, in the event of any such breach, in addition to such other remedies which may be available, the Executive shall have the right to specific performance and injunctive relief.

8.3 Governing Law. The validity, interpretation, construction and performance of this Agreement shall be governed by the internal laws of the Commonwealth of Massachusetts, without regard to conflicts of law principles.

8.4 Waivers. No waiver by the Executive at any time of any breach of, or compliance with, any provision of this Agreement to be performed by the Company shall be deemed a waiver of that or any other provision at any subsequent time.

8.5 Counterparts. This Agreement may be executed in counterparts, each of which shall be deemed to be an original but both of which together shall constitute one and the same instrument.

8.6 Tax Withholding. Any payments provided for hereunder shall be paid net of any applicable tax withholding required under federal, state or local law.

8.7 Entire Agreement. This Agreement sets forth the entire agreement of the parties hereto in respect of the subject matter contained herein and supersedes all prior agreements, promises, covenants, arrangements, communications, representations or warranties, whether oral or written, by any officer, employee or representative of any party hereto in respect of the subject matter contained herein; and any prior agreement of the parties hereto in respect of the subject matter contained herein is hereby terminated and cancelled.

8.8 Amendments. This Agreement may be amended or modified only by a written instrument executed by both the Company and the Executive.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first set forth above.

KĀDANT INC.

By: [Name]
[Title]

EXECUTIVE

[Name]

Exhibit 10.4

KADANT INC.

AMENDED AND RESTATED NONQUALIFIED STOCK OPTION PLAN

1. Purpose

This Nonqualified Stock Option Plan (the "Plan") is intended to encourage ownership of Common Stock (the "Common Stock"), of Kadant Inc. ("Company"), by persons selected by the Board of Directors (or a committee thereof) in its sole discretion, including directors, executive officers, key employees and consultants of the Company and its subsidiaries, and to provide additional incentive for them to promote the success of the business of the Company. The Plan is intended to be a nonstatutory stock option plan.

2. Effective Date of the Plan

The Plan shall become effective when adopted by the Board of Directors of the Company.

3. Stock Subject to Plan

Subject to adjustment as provided in Section 11, the total number of shares of Common Stock reserved and available for issuance under the Plan and the Company's Incentive Stock Option Plan in the aggregate shall be 720,000 shares. Shares to be issued upon the exercise of options granted under the Plan may be either authorized but unissued shares or shares held by the Company in its treasury. If any option expires or terminates for any reason without having been exercised in full, the unpurchased shares subject thereto shall again be available for options thereafter to be granted.

4. Administration

The Plan will be administered by the Board of Directors of the Company (the "Board"). Subject to the provisions of the Plan, the Board shall have complete authority, in its discretion, to make the following determinations with respect to each option to be granted by the Company: (a) the person to receive the option (the "Optionee"); (b) the time of granting the option; (c) the number of shares subject thereto; (d) the option price; (e) the option period; (f) the terms and conditions of options granted under the Plan (including terms and conditions relating to events of merger, consolidation, dissolution and liquidation, change of control, vesting, forfeiture, restrictions, dividends and interest, if any, on deferred amounts); (g) waive compliance by an optionee with any obligation to be performed by him or her under an option; (h) waive any term or condition of an option; (i) cancel an existing option in whole or in part with the consent of an Optionee; (j) grant replacement options; (k) accelerate the vesting or lapse of any restrictions of any option; and (l) adopt the form of instruments evidencing options under the Plan and change such forms from time to time. In making such determinations, the Board may take into account the nature of the services rendered by the Optionees, their present and potential contributions to the success of the Company and/or one or more of its subsidiaries, and such other factors as the Board in its discretion shall deem relevant. Subject to the provisions of the Plan, the Board shall also have complete authority to interpret the Plan, to prescribe, amend, and rescind rules and regulations relating to it, to determine the terms and provisions of the respective option agreements (which need not be identical), and to make all other determinations necessary or advisable for the administration of the Plan. Any interpretation by the Board of the terms and provisions of the Plan or any Award thereunder and the administration thereof, and all action taken by the Board, shall be final, binding and conclusive on all parties and any person claiming under or through any party. No Director shall be liable for any action or determination made in good faith. The Board may, to the full extent permitted by law, delegate any or all of its responsibilities under the Plan to a committee (the “Committee”) appointed by the Board and consisting of two or more members of the Board, each of whom shall be deemed a “disinterested person” within the meaning of Rule 16b-3 (or any successor rule) of the Securities Exchange Act of 1934 (the “Exchange Act”).

5. Eligibility

An option may be granted to any person selected by the Board in its sole discretion.

6. Time of Granting Options

The granting of an option shall take place at the time specified by the Board. Only if expressly so provided by the Board shall the granting of an option be regarded as taking place at the time when a written option agreement shall have been duly executed and delivered by or on behalf of the Company and the Optionee to whom such option shall be granted. The agreement shall provide, among other things, that it does not confer upon an Optionee any right to continue in the employ of the Company and/or one or more of its subsidiaries or to continue as a director or consultant of the Company, and that it does not interfere in any way with the right of the Company or any such subsidiary to terminate the employment of the Optionee at any time if the Optionee is an employee, to remove the Optionee as a director of the Company if the Optionee is a director, or to terminate the services of the Optionee if the Optionee is a consultant.

7. Option Period

An option may become exercisable immediately or in such installments, cumulative or noncumulative, as the Board may determine.

8. Exercise of Option

An option may be exercised in accordance with its terms by written notice of intent to exercise the option, specifying the number of shares of stock with respect to which the option is then being exercised. The notice shall be accompanied by payment in the form of cash or shares of Common Stock (the “Tendered Shares”) with a then current market value equal to the option price of the shares to be purchased; provided, however, that such Tendered Shares shall have been acquired by the Optionee more than six months prior to the date of exercise, unless such requirement is waived in writing by the Company. Against such payment the Company shall deliver or cause to be delivered to the Optionee a certificate for the number of shares then being purchased, registered in the name of the Optionee or other person exercising the option. If any law or applicable regulation of the Securities and Exchange Commission or other body having jurisdiction in the premises shall require the Company or the Optionee to take any action in connection with shares being purchased upon exercise of the option, exercise of the option and delivery of the certificate or certificates for such shares shall be postponed until completion of the necessary action, which shall be taken at the Company's expense.

9. Transferability

Except as may be authorized by the Board, in its sole discretion, no Option may be transferred other than by will or the laws of descent and distribution, and during a Optionee's lifetime an option requiring exercise may be exercised only by him or her (or in the event of incapacity, the person or persons properly appointed to act on his or her behalf). The Board may, in its discretion, determine the extent to which options granted to an Optionee shall be transferable, and such provisions permitting or acknowledging transfer shall be set forth in the written agreement evidencing the option executed and delivered by or on behalf of the Company and the Optionee.

10. Vesting, Restrictions and Termination of Options

The Board, in its sole discretion, may determine the manner in which options shall vest, the rights of the Company to repurchase the shares issued upon the exercise of any option and the manner in which such rights shall lapse, and the terms upon which any option granted shall terminate. The Board shall have the right to accelerate the date of exercise of any installment or to accelerate the lapse of the Company's repurchase rights. All of such terms shall be specified in a written option agreement executed and delivered by or on behalf of the Company and the Optionee to whom such option shall be granted.

11. Adjustments in the Event of Certain Transactions

(a) In the event of a stock dividend, stock split or combination of shares, or other distribution with respect to holders of Common Stock other than normal cash dividends, the Board will make (i) appropriate adjustments to the maximum number of shares that may be delivered under the Plan under Section 3 above, and (ii) appropriate adjustments to the number and kind of shares of stock or securities subject to Options then outstanding or subsequently granted, any exercise prices relating to Options and any other provisions of Awards affected by such change.

(b) In the event of any recapitalization, merger or consolidation involving the Company, any transaction in which the Company becomes a subsidiary of another entity, any sale or other disposition of all or a substantial portion of the assets of the Company or any similar transaction, as determined by the Board, the Board in its discretion may make appropriate adjustments to outstanding Options to avoid distortion in the operation of the Plan.

12. Change in Control

12.1 Impact of Event

In the event of a "Change in Control" as defined in Section 12.2 or Section 12.3, as applicable, the following provisions shall apply, unless the agreement evidencing the Award otherwise provides (by specific explicit reference to Section 12.2 and Section 12.3 below). If a Change in Control occurs while any Awards are outstanding, then, effective upon the Change in Control, (i) each outstanding stock option or other stock-based Award awarded under the Plan that was not previously exercisable and vested shall become immediately exercisable in full and vested, and will no longer be subject to a right of repurchase by the Company, (ii) each outstanding restricted stock award or other stock-based Award subject to restrictions and to the extent not fully vested, shall be deemed to be fully vested, free of restrictions and conditions and no longer subject to a right of repurchase by the Company, and (iii) deferral limitations and conditions that relate solely to the passage of time, continued employment or affiliation will be waived and removed as to deferred stock Awards and performance Awards; performance of other conditions (other than conditions relating solely to the passage of time, continued employment or affiliation) will continue to apply unless otherwise provided in the agreement evidencing the Award or in any other agreement between the Optionee and the Company or unless otherwise agreed by the Board.

12.2 Definition of "Change in Control" Prior to the Spin-Off

"Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below that occurs prior to the distribution of all or substantially all of the shares of Common Stock held beneficially by Thermo Electron Corporation in a tax-free spin-off under Section 355 of the Code (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Person") of beneficial ownership of any capital stock of Thermo Electron Corporation ("Thermo Electron") if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 40% or more of either (i) the then-outstanding shares of common stock of Thermo Electron (the "Outstanding TMO Common Stock") or (ii) the combined voting power of the then-outstanding securities of Thermo Electron entitled to vote generally in the election of directors (the "Outstanding TMO Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions shall not constitute a Change in Control: (i) any acquisition by Thermo Electron, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by Thermo Electron or any corporation controlled by Thermo Electron, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board of Directors of Thermo Electron (the "Thermo Board") (or, if applicable, the Board of Directors of a successor corporation to Thermo Electron), where the term “Continuing Director” means at any date a member of the Thermo Board (i) who was a member of the Thermo Board as of July 1, 1999 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Thermo Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Thermo Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving Thermo Electron or a sale or other disposition of all or substantially all of the assets of Thermo Electron in one or a series of transactions (a “Business Combination”), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding TMO Common Stock and Outstanding TMO Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 60% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns Thermo Electron or substantially all of Thermo Electron’s assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the “Acquiring Corporation”) in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding TMO Common Stock and Outstanding TMO Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by Thermo Electron or by the Acquiring Corporation) beneficially owns, directly or indirectly, 40% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of Thermo Electron of a complete liquidation or dissolution of Thermo Electron.

12.3 Definition of “Change in Control” Upon Spin-Off

“Change in Control” means an event or occurrence set forth in any one or more of subsections (a) through (d) below that occurs on or after the distribution of all or substantially all of the shares of Common Stock held beneficially by Thermo Electron Corporation in a tax-free spin-off under Section 355 of the Code (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection) (references to Section 12.2 in written option agreements shall be deemed to refer to this Section 12.3 after the date of said spin-off):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a “Person”) of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 40% or more of either (i) the then-outstanding shares of common stock of the Company (the “Outstanding Common Stock”) or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the “Outstanding Voting Securities”); provided, however, that for purposes of this subsection (a), the following acquisitions of shares of Common Stock shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the board of directors of a successor corporation to the Company), where the term “Continuing Director” means at any date a member of the Board (i) who was a member of the Board as of July 1, 1999 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a “Business Combination”), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Common Stock and Outstanding Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 60% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company’s assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the “Acquiring Corporation”) in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Common Stock and Outstanding Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 40% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

13. Limitation of Rights in Option Stock

The Optionees shall have no rights as stockholders in respect of shares as to which their options shall not have been exercised, certificates issued and delivered and payment as herein provided made in full, and shall have no rights with respect to such shares not expressly conferred by this Plan.

14. Stock Reserved

The Company shall at all times during the term of the options reserve and keep available such number of shares of the Common Stock as will be sufficient to satisfy the requirements of this Plan and shall pay all other fees and expenses necessarily incurred by the Company in connection therewith.

15. Securities Laws Restrictions

Each Optionee exercising an option, at the request of the Company, will be required to give a representation in form satisfactory to counsel for the Company that he will not transfer, sell or otherwise dispose of the shares received upon exercise of the option at any time purchased by him, upon exercise of any portion of the option, in a manner which would violate the Securities Act of 1933, as amended, and the regulations of the Securities and Exchange Commission thereunder and the Company may, if required or at its discretion, make a notation on any certificates issued upon exercise of options to the effect that such certificate may not be transferred except after receipt by the Company of an opinion of counsel satisfactory to it to the effect that such transfer will not violate such Act and such regulations.

16. Tax Withholding

The Company shall have the right to deduct from payments of any kind otherwise due to an Optionee any federal, state or local taxes of any kind required by law to be withheld with respect to any shares issued upon exercise of options under the Plan (the "withholding requirements"). The Board will have the right to require that the Optionee or other appropriate person remit to the Company an amount sufficient to satisfy the withholding requirements, or make other arrangements satisfactory to the Board with regard to such requirements, prior to the delivery of any Common Stock pursuant to exercise of an option. If and to the extent that such withholding is required, the Board may permit the Optionee or such other person to elect at such time and in such manner as the Board provides to have the Company hold back from the shares to be delivered, or to deliver to the Company, Common Stock having a value calculated to satisfy the withholding requirements.

17. Termination and Amendment

The Plan shall remain in full force and effect until terminated by the Board. Subject to the last sentence of the first paragraph of this Section 17, the Board may at any time or times amend the Plan or any outstanding Option for any purpose that may at the time be permitted by law, or may at any time terminate the Plan as to any further grants of Options. No amendment of the Plan or any agreement evidencing Options under the Plan may adversely affect the rights of any participant under any Option previously granted without such participant's consent.

Notwithstanding any other provisions hereof, the Plan shall terminate on December 28, 2001 and no options shall be granted hereunder thereafter.

18. Compliance with Section 409A of the Code

To the extent applicable to an Option, it is intended that this Plan and Options made under the Plan comply with the provisions of Section 409A of the Internal Revenue Code, as amended (the "Code") and applicable rules and regulations. The Plan and any Options to which Section 409A is applicable will be administered in a manner consistent with this intent, and any provision that would cause this Plan or any Option made under the Plan to fail to satisfy Section 409A of the Code, to the extent applicable, shall have no force and effect until amended to comply with Section 409A of the Code (which amendment may be retroactive to the extent permitted by Section 409A and may be made by the Company without the consent of Optionees to which Section 409A shall apply).

Except as provided in individual Option agreements initially or by amendment, if and to the extent any portion of any payment, compensation or other benefit provided to a Optionee in connection with his or her employment termination is determined to constitute "nonqualified deferred compensation" within the meaning of Section 409A of the Code and the Optionee is a specified employee as defined in Section 409A(a)(2)(B)(i) of the Code, as determined by the Company in accordance with its procedures, by which determination the Optionee (through accepting the Option) agrees that he or she is bound, such portion of the payment, compensation or other benefit shall not be paid before the day that is six months plus one day after the date of "separation from service" (as determined under Code Section 409A) (the "***New Payment Date***"), except as Code Section 409A may then permit. The aggregate of any payments that otherwise would have been paid to the Optionee during the period between the date of separation from service and the New Payment Date shall be paid to the Optionee in a lump sum on such New Payment Date, and any remaining payments will be paid on their original schedule.

The Company makes no representations or warranty and shall have no liability to the Optionee or any other person if any provisions of or payments, compensation or other benefits under the Plan are determined to constitute nonqualified deferred compensation subject to Section 409A of the Code but do not to satisfy the conditions of that section.

KADANT INC.

AMENDED AND RESTATED EQUITY INCENTIVE PLAN

1. Purpose

The purpose of this Equity Incentive Plan (the "Plan") is to secure for Kadant Inc. (the "Company") and its Stockholders the benefits arising from capital stock ownership by employees, officers and directors of, and consultants to, the Company and its subsidiaries or other persons who are expected to make significant contributions to the future growth and success of the Company and its subsidiaries. The Plan is intended to accomplish these goals by enabling the Company to offer such persons equity-based interests, equity-based incentives or performance-based stock incentives in the Company, or any combination thereof ("Awards").

2. Administration

The Plan will be administered by the Board of Directors of the Company (the "Board"). The Board shall have full power to interpret and administer the Plan, to prescribe, amend and rescind rules and regulations relating to the Plan and Awards, and full authority to select the persons to whom Awards will be granted ("Participants"), determine the type and amount of Awards to be granted to Participants (including any combination of Awards), determine the terms and conditions of Awards granted under the Plan (including terms and conditions relating to events of merger, consolidation, dissolution and liquidation, change of control, vesting, forfeiture, restrictions, dividends and interest, if any, on deferred amounts), waive compliance by a participant with any obligation to be performed by him or her under an Award, waive any term or condition of an Award, cancel an existing Award in whole or in part with the consent of a Participant, grant replacement Awards, accelerate the vesting or lapse of any restrictions of any Award, correct any defect, supply any omission or reconcile any inconsistency in the Plan or in any award and adopt the form of instruments evidencing Awards under the Plan and change such forms from time to time. Any interpretation by the Board of the terms and provisions of the Plan or any Award thereunder and the administration thereof, and all action taken by the Board, shall be final, binding and conclusive on all parties and any person claiming under or through any party. No Director shall be liable for any action or determination made in good faith. The Board may, to the full extent permitted by law, delegate any or all of its responsibilities under the Plan to a committee (the "Committee") appointed by the Board and consisting of members of the Board. All references in the Plan to the "Board" shall mean the Board or a Committee of the Board to the extent that the Board's powers or authority under the Plan have been delegated to such Committee.

3. Effective Date

The Plan shall be effective as of the date first approved by the Board, subject to the approval of the Plan by the Company's stockholders. Grants of Awards under the Plan made prior to such approval shall be effective when made (unless otherwise specified by the Board at the time of grant), but shall be conditioned on and subject to such approval of the Plan.

4. **Shares Subject to the Plan**

Subject to adjustment as provided in Section 10.6, the total number of shares of common stock of the Company, par value $.01 per share (the "Common Stock"), reserved and available for distribution under the Plan shall be 2,050,000 shares. Such shares may consist, in whole or in part, of authorized and unissued shares or treasury shares.

If any Award of shares of Common Stock requiring exercise by the Participant for delivery of such shares expires or terminates without having been exercised in full, is forfeited or is otherwise terminated without a payment being made to the Participant in the form of Common Stock, or if any shares of Common Stock subject to restrictions are repurchased by the Company pursuant to the terms of any Award or are otherwise reacquired by the Company to satisfy obligations arising by virtue of any Award, such shares shall be available for distribution in connection with future Awards under the Plan, subject, however, in the case of Incentive Stock Options (as hereinafter defined), to any limitations under the Code.

5. **Eligibility**

Employees, officers and directors of, and consultants to, the Company and its subsidiaries, or other persons who are expected to make significant contributions to the future growth and success of the Company and its subsidiaries shall be eligible to receive Awards under the Plan. The Board, or other appropriate committee or person to the extent permitted pursuant to the last sentence of Section 2, shall from time to time select from among such eligible persons those who will receive Awards under the Plan.

6. **Types of Awards**

The Board may offer Awards under the Plan in any form of equity-based interest, equity-based incentive or performance-based stock incentive in Common Stock of the Company or any combination thereof. The type, terms and conditions and restrictions of an Award shall be determined by the Board at the time such Award is made to a Participant; provided however that the maximum number of shares permitted to be granted under any Award or combination of Awards to any Participant during any one calendar year may not exceed 500,000 shares of Common Stock, subject to adjustment as provided under Section 10.6.

An Award shall be made at the time specified by the Board, shall be subject to such conditions or restrictions as may be imposed by the Board and shall conform to the general rules applicable under the Plan as well as any special rules then applicable under federal tax laws or regulations or the federal securities laws relating to the type of Award granted.

Without limiting the foregoing, Awards may take the following forms and shall be subject to the following rules and conditions:

6.1 Options

An option is an Award that entitles the holder on exercise thereof to purchase Common Stock at a specified exercise price. Options granted under the Plan may be either incentive stock options ("incentive stock options") that meet the requirements of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), or options that are not intended to meet the requirements of Section 422 of the Code ("non-statutory options").

6.1.1 Option Price. The price at which Common Stock may be purchased upon exercise of an option shall be determined by the Board, provided however, the exercise price shall not be less than 85% of the fair market value per share of Common Stock as of the date of grant.

6.1.2 Option Grants. The granting of an option shall take place at the time specified by the Board. Options shall be evidenced by option agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including but not limited to vesting and forfeiture provisions, acceleration, change of control, protection in the event of merger, consolidations, dissolutions and liquidations) as the Board shall deem advisable. Option agreements shall expressly state whether an option grant is intended to qualify as an incentive stock option or non-statutory option.

6.1.3 Option Period. An option will become exercisable at such time or times (which may be immediately or in such installments as the Board shall determine) and on such terms and conditions as the Board shall specify. The option agreements shall specify the terms and conditions applicable in the event of an option holder's termination of employment during the option's term.

Any exercise of an option must be in writing, signed by the proper person and delivered or mailed to the Company, accompanied by (1) any additional documents required by the Board and (2) payment in full in accordance with Section 6.1.4 for the number of shares for which the option is exercised.

6.1.4 Payment of Exercise Price. Stock purchased on exercise of an option shall be paid for as follows: (1) in cash or by check (subject to such guidelines as the Company may establish for this purpose), bank draft or money order payable to the order of the Company or (2) if so permitted by the instrument evidencing the option (or in the case of a non-statutory option, by the Board at or after grant of the option), (i) through the delivery of shares of Common Stock that have been outstanding for at least six months (unless the Board expressly approves a shorter period) and that have a fair market value (determined in accordance with procedures prescribed by the Board) equal to the exercise price, (ii) by delivery of a promissory note of the option holder to the Company, payable on such terms as are specified by the Board, (iii) by delivery of an unconditional and irrevocable undertaking by a broker to deliver promptly to the Company sufficient funds to pay the exercise price, or (iv) by any combination of the foregoing permissible forms of payment.

6.1.5 Buyout Provision. The Board may at any time offer to buy out for a payment in cash, shares of Common Stock, deferred stock or restricted stock, an option previously granted, based on such terms and conditions as the Board shall establish and communicate to the option holder at the time that such offer is made.

6.1.6 Special Rules for Incentive Stock Options. Each provision of the Plan and each option agreement evidencing an incentive stock option shall be construed so that each incentive stock option shall be an incentive stock option as defined in Section 422 of the Code or any statutory provision that may replace such Section, and any provisions thereof that cannot be so construed shall be disregarded. Instruments evidencing incentive stock options shall contain such provisions as are required under applicable provisions of the Code. Incentive stock options may be granted only to employees of the Company and its subsidiaries. The exercise price of an incentive stock option shall not be less than 100% (110% in the case of an incentive stock option granted to a more than ten percent Stockholder of the Company) of the fair market value of the Common Stock on the date of grant, as determined by the Board. An incentive stock option may not be granted after the tenth anniversary of the date on which the Plan was adopted by the Board and the latest date on which an incentive stock option may be exercised shall be the tenth anniversary (fifth anniversary, in the case of any incentive stock option granted to a more than ten percent Stockholder of the Company) of the date of grant, as determined by the Board.

6.2 Restricted and Unrestricted Stock

An Award of restricted stock entitles the recipient thereof to acquire shares of Common Stock upon payment of the purchase price subject to restrictions specified in the instrument evidencing the Award.

6.2.1 Restricted Stock Awards. Awards of restricted stock shall be evidenced by restricted stock agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including restriction and forfeiture provisions, change of control, protection in the event of mergers, consolidations, dissolutions and liquidations) as the Board shall deem advisable.

6.2.2 Restrictions. Until the restrictions specified in a restricted stock agreement shall lapse, restricted stock may not be sold, assigned, transferred, pledged or otherwise encumbered or disposed of, and upon certain conditions specified in the restricted stock agreement, must be resold to the Company for the price, if any, specified in such agreement. The restrictions shall lapse at such time or times, and on such conditions, as the Board may specify. The Board may at any time accelerate the time at which the restrictions on all or any part of the shares shall lapse.

6.2.3 Rights as a Stockholder. A Participant who acquires shares of restricted stock will have all of the rights of a Stockholder with respect to such shares including the right to receive dividends and to vote such shares. Unless the Board otherwise determines, certificates evidencing shares of restricted stock will remain in the possession of the Company until such shares are free of all restrictions under the Plan.

6.2.4 **Purchase Price**. The purchase price of shares of restricted stock shall be determined by the Board, in its sole discretion.

6.2.5 **Other Awards Settled With Restricted Stock**. The Board may provide that any or all the Common Stock delivered pursuant to an Award will be restricted stock.

6.2.6 **Unrestricted Stock.** The Board may, in its sole discretion, sell to any Participant shares of Common Stock free of restrictions under the Plan for a price determined by the Board, but which may not be less than the par value per share of the Common Stock.

6.3 **Deferred Stock**

6.3.1 **Deferred Stock Award.** A deferred stock Award entitles the recipient to receive shares of deferred stock, which is Common Stock to be delivered in the future. Delivery of the Common Stock will take place at such time or times, and on such conditions, as the Board may specify. The Board may at any time accelerate the time at which delivery of all or any part of the Common Stock will take place.

6.3.2 **Other Awards Settled with Deferred Stock.** The Board may, at the time any Award described in this Section 6 is granted, provide that, at the time Common Stock would otherwise be delivered pursuant to the Award, the Participant will instead receive an instrument evidencing the right to future delivery of deferred stock.

6.4 **Performance Awards**

6.4.1 **Performance Awards**. A performance Award entitles the recipient to receive, without payment, an amount, in cash or Common Stock or a combination thereof (such form to be determined by the Board), following the attainment of performance goals. Performance goals may be related to personal performance, corporate performance, departmental performance or any other category of performance deemed by the Board to be important to the success of the Company. The Board will determine the performance goals, the period or periods during which performance is to be measured and all other terms and conditions applicable to the Award.

6.4.2 **Other Awards Subject to Performance Conditions**. The Board may, at the time any Award described in this Section 6 is granted, impose a condition or conditions (in addition to any conditions specified or authorized in this Section 6 of the Plan) that performance goals be met prior to the Participant's realization of any payment or benefit under the Award.

7. **Purchase Price and Payment**

Except as otherwise provided in the Plan, the purchase price of Common Stock to be acquired pursuant to an Award shall be the price determined by the Board, provided that such price shall not be less than the par value of the Common Stock. Except as otherwise provided in the Plan, the Board may determine the method of payment of the exercise price or purchase price of an Award granted under the Plan and the form of payment. The Board may determine that all or any part of the purchase price of Common Stock pursuant to an Award has been satisfied by past services rendered by the Participant. The Board may agree at any time, upon request of the Participant, to defer the date on which any payment under an Award will be made.

8. Loans and Supplemental Grants

The Company may make a loan to a Participant, either on or after the grant to the Participant of any Award, in connection with the purchase of Common Stock under the Award or with the payment of any obligation incurred or recognized as a result of the Award. The Board will have full authority to decide whether the loan is to be secured or unsecured or with or without recourse against the borrower, the terms on which the loan is to be repaid and the conditions, if any, under which it may be forgiven.

In connection with any Award, the Board may at the time such Award is made or at a later date, provide for and make a cash payment to the participant not to exceed an amount equal to (a) the amount of any federal, state and local income tax or ordinary income for which the Participant will be liable with respect to the Award, plus (b) an additional amount on a grossed-up basis necessary to make him or her whole after tax, discharging all the participant's income tax liabilities arising from all payments under the Plan.

9. Change in Control

9.1 Impact of Event

In the event of a "Change in Control" as defined in Section 9.2 or Section 9.3, as applicable, the following provisions shall apply, unless the agreement evidencing the Award otherwise provides (by specific explicit reference to Section 9.2 and Section 9.3 below). If a Change in Control occurs while any Awards are outstanding, then, effective upon the Change in Control, (i) each outstanding stock option or other stock-based Award awarded under the Plan that was not previously exercisable and vested shall become immediately exercisable in full and vested, and will no longer be subject to a right of repurchase by the Company, (ii) each outstanding restricted stock award or other stock-based Award subject to restrictions and to the extent not fully vested, shall be deemed to be fully vested, free of restrictions and conditions and no longer subject to a right of repurchase by the Company, and (iii) deferral limitations and conditions that relate solely to the passage of time, continued employment or affiliation will be waived and removed as to deferred stock Awards and performance Awards; performance of other conditions (other than conditions relating solely to the passage of time, continued employment or affiliation) will continue to apply unless otherwise provided in the agreement evidencing the Award or in any other agreement between the Participant and the Company or unless otherwise agreed by the Board.

9.2 Definition of "Change in Control" Prior to the Spin-Off

"Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below that occurs prior to the distribution of all or substantially all of the shares of Common Stock held beneficially by Thermo Electron Corporation in a tax-free spin-off under Section 355 of the Code (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Person") of beneficial ownership of any capital stock of Thermo Electron Corporation ("Thermo Electron") if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 40% or more of either (i) the then-outstanding shares of common stock of Thermo Electron (the "Outstanding TMO Common Stock") or (ii) the combined voting power of the then-outstanding securities of Thermo Electron entitled to vote generally in the election of directors (the "Outstanding TMO Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions shall not constitute a Change in Control: (i) any acquisition by Thermo Electron, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by Thermo Electron or any corporation controlled by Thermo Electron, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board of Directors of Thermo Electron (the "Thermo Board") (or, if applicable, the Board of Directors of a successor corporation to Thermo Electron), where the term "Continuing Director" means at any date a member of the Thermo Board (i) who was a member of the Thermo Board as of July 1, 1999 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Thermo Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Thermo Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving Thermo Electron or a sale or other disposition of all or substantially all of the assets of Thermo Electron in one or a series of transactions (a "Business Combination"), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding TMO Common Stock and Outstanding TMO Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 60% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns Thermo Electron or substantially all of Thermo Electron's assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the "Acquiring Corporation") in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding TMO Common Stock and Outstanding TMO Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by Thermo Electron or by the Acquiring Corporation) beneficially owns, directly or indirectly, 40% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of Thermo Electron of a complete liquidation or dissolution of Thermo Electron.

9.3 Definition of "Change in Control" Upon Spin-Off

"Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below that occurs on or after the distribution of all or substantially all of the shares of Common Stock held beneficially by Thermo Electron Corporation in a tax-free spin-off under Section 355 of the Code (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection) (references to Section 9.2 in written option agreements shall be deemed to refer to this Section 9.3 after the date of said spin-off):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Person") of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 40% or more of either (i) the then-outstanding shares of common stock of the Company (the "Outstanding Common Stock") or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the "Outstanding Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions of shares of Common Stock shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the board of directors of a successor corporation to the Company), where the term "Continuing Director" means at any date a member of the Board (i) who was a member of the Board as of May 23, 1994 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a “Business Combination”), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Common Stock and Outstanding Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 60% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company’s assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the “Acquiring Corporation”) in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Common Stock and Outstanding Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 40% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

10. General Provisions

10.1 Documentation of Awards

Awards will be evidenced by written instruments, which may differ among Participants, prescribed by the Board from time to time. Such instruments may be in the form of agreements to be executed by both the Participant and the Company or certificates, letters or similar instruments which need not be executed by the participant but acceptance of which will evidence agreement to the terms thereof. Such instruments shall conform to the requirements of the Plan and may contain such other provisions (including provisions relating to events of merger, consolidation, dissolution and liquidations, change of control and restrictions affecting either the agreement or the Common Stock issued thereunder), as the Board deems advisable.

10.2 Rights as a Stockholder

Except as specifically provided by the Plan or the instrument evidencing the Award, the receipt of an Award will not give a Participant rights as a Stockholder with respect to any shares covered by an Award until the date of issue of a stock certificate to the participant for such shares.

10.3 Conditions on Delivery of Stock

The Company will not be obligated to deliver any shares of Common Stock pursuant to the Plan or to remove any restriction from shares previously delivered under the Plan (a) until all conditions of the Award have been satisfied or removed, (b) until, in the opinion of the Company's counsel, all applicable federal and state laws and regulations have been complied with, (c) if the outstanding Common Stock is at the time listed on any stock exchange, until the shares have been listed or authorized to be listed on such exchange upon official notice of issuance, and (d) until all other legal matters in connection with the issuance and delivery of such shares have been approved by the Company's counsel. If the sale of Common Stock has not been registered under the Securities Act of 1933, as amended, the Company may require, as a condition to exercise of the Award, such representations or agreements as counsel for the Company may consider appropriate to avoid violation of such act and may require that the certificates evidencing such Common Stock bear an appropriate legend restricting transfer.

If an Award is exercised by the participant's legal representative, the Company will be under no obligation to deliver Common Stock pursuant to such exercise until the Company is satisfied as to the authority of such representative.

10.4 Tax Withholding

The Company will withhold from any cash payment made pursuant to an Award an amount sufficient to satisfy all federal, state and local withholding tax requirements (the "withholding requirements").

In the case of an Award pursuant to which Common Stock may be delivered, the Board will have the right to require that the participant or other appropriate person remit to the Company an amount sufficient to satisfy the withholding requirements, or make other arrangements satisfactory to the Board with regard to such requirements, prior to the delivery of any Common Stock. If and to the extent that such withholding is required, the Board may permit the participant or such other person to elect at such time and in such manner as the Board provides to have the Company hold back from the shares to be delivered, or to deliver to the Company, Common Stock having a value calculated to satisfy the withholding requirement.

10.5 Transferability of Awards

Except as may be authorized by the Board, in its sole discretion, no Award (other than an Award in the form of an outright transfer of cash or Common Stock not subject to any restrictions) may be sold, assigned, transferred, pledged or otherwise encumbered other than by will or the laws of descent and distribution, and during a Participant's lifetime an Award requiring exercise may be exercised only by him or her (or in the event of incapacity, the person or persons properly appointed to act on his or her behalf). The Board may, in its discretion, determine the extent to which Awards granted to a Participant shall be transferable, and such provisions permitting or acknowledging transfer shall be set forth in the written agreement evidencing the Award executed and delivered by or on behalf of the Company and the Participant.

10.6 Adjustments in the Event of Certain Transactions

(a) In the event of a stock dividend, stock split or combination of shares, or other distribution with respect to holders of Common Stock other than normal cash dividends, the Board will make (i) appropriate adjustments to the maximum number of shares that may be delivered under the Plan under Section 4 above and the participant limit set forth in Section 6, and (ii) appropriate adjustments to the number and kind of shares of stock or securities subject to Awards then outstanding or subsequently granted, any exercise prices relating to Awards and any other provisions of Awards affected by such change.

(b) In the event of any recapitalization, merger or consolidation involving the Company, any transaction in which the Company becomes a subsidiary of another entity, any sale or other disposition of all or a substantial portion of the assets of the Company or any similar transaction, as determined by the Board, the Board in its discretion may make appropriate adjustments to outstanding Awards to avoid distortion in the operation of the Plan.

10.7 <u>Employment Rights</u>

Neither the adoption of the Plan nor the grant of Awards will confer upon any person any right to continued employment with the Company or any subsidiary or interfere in any way with the right of the Company or subsidiary to terminate any employment relationship at any time or to increase or decrease the compensation of such person. Except as specifically provided by the Board in any particular case, the loss of existing or potential profit in Awards granted under the Plan will not constitute an element of damages in the event of termination of an employment relationship even if the termination is in violation of an obligation of the Company to the employee.

Whether an authorized leave of absence, or absence in military or government service, shall constitute termination of employment shall be determined by the Board at the time. For purposes of this Plan, transfer of employment between the Company and its subsidiaries shall not be deemed termination of employment.

10.8 <u>Other Employee Benefits</u>

The value of an Award granted to a Participant who is an employee, and the amount of any compensation deemed to be received by an employee as a result of any exercise or purchase of Common Stock pursuant to an Award or sale of shares received under the Plan, will not constitute “earnings” or “compensation” with respect to which any other employee benefits of such employee are determined, including without limitation benefits under any pension, stock ownership, stock purchase, life insurance, medical, health, disability or salary continuation plan.

10.9 <u>Legal Holidays</u>

If any day on or before which action under the Plan must be taken falls on a Saturday, Sunday or legal holiday, such action may be taken on the next succeeding day not a Saturday, Sunday or legal holiday.

10.10 Foreign Nationals

Without amending the Plan, Awards may be granted to persons who are foreign nationals or employed outside the United States or both, on such terms and conditions different from those specified in the Plan, as may, in the judgment of the Board, be necessary or desirable to further the purpose of the Plan.

10.11 Governing Law

The provisions of the Plan and all Awards made hereunder shall be governed by and interpreted in accordance with the laws of the State of Delaware, without regard to any applicable conflicts of law.

11. Termination and Amendment

The Plan shall remain in full force and effect until terminated by the Board. Subject to the last sentence of this Section 11, the Board may at any time or times amend the Plan or any outstanding Award for any purpose that may at the time be permitted by law, or may at any time terminate the Plan as to any further grants of Awards. No amendment of the Plan or any agreement evidencing Awards under the Plan may adversely affect the rights of any participant under any Award previously granted without such participant's consent.

12. Compliance with Section 409A of the Code

To the extent applicable to an Award, it is intended that this Plan and Awards made under the Plan comply with the provisions of Section 409A of the Code and applicable rules and regulations. The Plan and any Awards to which Section 409A is applicable will be administered in a manner consistent with this intent, and any provision that would cause this Plan or any Award made under the Plan to fail to satisfy Section 409A of the Code, to the extent applicable, shall have no force and effect until amended to comply with Section 409A of the Code (which amendment may be retroactive to the extent permitted by Section 409A and may be made by the Company without the consent of Participants to which Section 409A shall apply).

Except as provided in individual Award agreements initially or by amendment, if and to the extent any portion of any payment, compensation or other benefit provided to a Participant in connection with his or her employment termination is determined to constitute "nonqualified deferred compensation" within the meaning of Section 409A of the Code and the Participant is a specified employee as defined in Section 409A(a)(2)(B)(i) of the Code, as determined by the Company in accordance with its procedures, by which determination the Participant (through accepting the Award) agrees that he or she is bound, such portion of the payment, compensation or other benefit shall not be paid before the day that is six months plus one day after the date of "separation from service" (as determined under Code Section 409A) (the "***New Payment Date***"), except as Code Section 409A may then permit. The aggregate of any payments that otherwise would have been paid to the Participant during the period between the date of separation from service and the New Payment Date shall be paid to the Participant in a lump sum on such New Payment Date, and any remaining payments will be paid on their original schedule.

The Company makes no representations or warranty and shall have no liability to the Participant or any other person if any provisions of or payments, compensation or other benefits under the Plan are determined to constitute nonqualified deferred compensation subject to Section 409A of the Code but do not to satisfy the conditions of that section.

As amended and in effect as of 12/09/08

Exhibit 10.6

KADANT INC.

2001 EMPLOYEES EQUITY INCENTIVE PLAN

1. Purpose

The purpose of this 2001 Employees Equity Incentive Plan (the "Plan") is to secure for Kadant Inc. (the "Company") and its Stockholders the benefits arising from capital stock ownership by employees and consultants to the Company and its subsidiaries or other persons who are expected to make significant contributions to the future growth and success of the Company and its subsidiaries. The Plan is intended to accomplish these goals by enabling the Company to offer such persons equity-based interests, equity-based incentives or performance-based stock incentives in the Company, or any combination thereof ("Awards").

2. Administration

The Plan will be administered by the Board of Directors of the Company (the "Board"). The Board shall have full power to interpret and administer the Plan, to prescribe, amend and rescind rules and regulations relating to the Plan and Awards, and full authority to select the persons to whom Awards will be granted ("Participants"), determine the type and amount of Awards to be granted to Participants (including any combination of Awards), determine the terms and conditions of Awards granted under the Plan (including terms and conditions relating to events of merger, consolidation, dissolution and liquidation, change of control, vesting, forfeiture, restrictions, dividends and interest, if any, on deferred amounts), waive compliance by a participant with any obligation to be performed by him or her under an Award, waive any term or condition of an Award, cancel an existing Award in whole or in part with the consent of a Participant, grant replacement Awards, accelerate the vesting or lapse of any restrictions of any Award, correct any defect, supply any omission or reconcile any inconsistency in the Plan or in any award and adopt the form of instruments evidencing Awards under the Plan and change such forms from time to time. Any interpretation by the Board of the terms and provisions of the Plan or any Award thereunder and the administration thereof, and all action taken by the Board, shall be final, binding and conclusive on all parties and any person claiming under or through any party. No Director shall be liable for any action or determination made in good faith. The Board may, to the full extent permitted by law, delegate any or all of its responsibilities under the Plan to a committee (the "Committee") appointed by the Board and consisting of members of the Board. All references in the Plan to the "Board" shall mean the Board or a Committee of the Board to the extent that the Board's powers or authority under the Plan have been delegated to such Committee.

3. Effective Date

The Plan shall be effective as of the date first approved by the Board.

4. Shares Subject to the Plan

Subject to adjustment as provided in Section 10.6, the total number of shares of common stock of the Company, par value $.01 per share (the "Common Stock"), reserved and available for distribution under the Plan shall be 612,000 shares. Such shares may consist, in whole or in part, of authorized and unissued shares or treasury shares.

If any Award of shares of Common Stock requiring exercise by the Participant for delivery of such shares expires or terminates without having been exercised in full, is forfeited or is otherwise terminated without a payment being made to the Participant in the form of Common Stock, or if any shares of Common Stock subject to restrictions are repurchased by the Company pursuant to the terms of any Award or are otherwise reacquired by the Company to satisfy obligations arising by virtue of any Award, such shares shall be available for distribution in connection with future Awards under the Plan.

5. Eligibility

Employees and consultants to the Company and its subsidiaries, or other persons who are expected to make significant contributions to the future growth and success of the Company and its subsidiaries shall be eligible to receive Awards under the Plan. Executive officers and directors shall not be eligible to receive Awards under the Plan. The Board, or other appropriate committee or person to the extent permitted pursuant to the last sentence of Section 2, shall from time to time select from among such eligible persons those who will receive Awards under the Plan.

6. Types of Awards

The Board may offer Awards under the Plan in any form of equity-based interest, equity-based incentive or performance-based stock incentive in Common Stock of the Company or any combination thereof. The type, terms and conditions and restrictions of an Award shall be determined by the Board at the time such Award is made to a Participant.

An Award shall be made at the time specified by the Board, shall be subject to such conditions or restrictions as may be imposed by the Board and shall conform to the general rules applicable under the Plan as well as any special rules then applicable under federal tax laws or regulations or the federal securities laws relating to the type of Award granted.

Without limiting the foregoing, Awards may take the following forms and shall be subject to the following rules and conditions:

6.1 Options

An option is an Award that entitles the holder on exercise thereof to purchase Common Stock at a specified exercise price. Options granted under the Plan are not intended to meet the requirements of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code").

6.1.1 __**Option Price**__. The price at which Common Stock may be purchased upon exercise of an option shall be determined by the Board.

6.1.2 __**Option Grants**__. The granting of an option shall take place at the time specified by the Board. Options shall be evidenced by option agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including but not limited to vesting and forfeiture provisions, acceleration, change of control, protection in the event of merger, consolidations, dissolutions and liquidations) as the Board shall deem advisable. Option agreements shall expressly state whether an option grant is intended to qualify as an incentive stock option or non-statutory option.

6.1.3 __**Option Period**__. An option will become exercisable at such time or times (which may be immediately or in such installments as the Board shall determine) and on such terms and conditions as the Board shall specify. The option agreements shall specify the terms and conditions applicable in the event of an option holder's termination of employment during the option's term.

Any exercise of an option must be in writing, signed by the proper person and delivered or mailed to the Company, accompanied by (1) any additional documents required by the Board and (2) payment in full in accordance with Section 6.1.4 for the number of shares for which the option is exercised.

6.1.4 __**Payment of Exercise Price**__. Stock purchased on exercise of an option shall be paid for as follows: (1) in cash or by check (subject to such guidelines as the Company may establish for this purpose), bank draft or money order payable to the order of the Company or (2) if so permitted by the instrument evidencing the option (or in the case of a non-statutory option, by the Board at or after grant of the option), (i) through the delivery of shares of Common Stock that have been outstanding for at least six months (unless the Board expressly approves a shorter period) and that have a fair market value (determined in accordance with procedures prescribed by the Board) equal to the exercise price, (ii) by delivery of a promissory note of the option holder to the Company, payable on such terms as are specified by the Board, (iii) by delivery of an unconditional and irrevocable undertaking by a broker to deliver promptly to the Company sufficient funds to pay the exercise price, or (iv) by any combination of the foregoing permissible forms of payment.

6.1.5 __**Buyout Provision**__. The Board may at any time offer to buy out for a payment in cash, shares of Common Stock, deferred stock or restricted stock, an option previously granted, based on such terms and conditions as the Board shall establish and communicate to the option holder at the time that such offer is made.

6.2 __Restricted and Unrestricted Stock__

An Award of restricted stock entitles the recipient thereof to acquire shares of Common Stock upon payment of the purchase price subject to restrictions specified in the instrument evidencing the Award.

6.2.1 Restricted Stock Awards. Awards of restricted stock shall be evidenced by restricted stock agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including restriction and forfeiture provisions, change of control, protection in the event of mergers, consolidations, dissolutions and liquidations) as the Board shall deem advisable.

6.2.2 Restrictions. Until the restrictions specified in a restricted stock agreement shall lapse, restricted stock may not be sold, assigned, transferred, pledged or otherwise encumbered or disposed of, and upon certain conditions specified in the restricted stock agreement, must be resold to the Company for the price, if any, specified in such agreement. The restrictions shall lapse at such time or times, and on such conditions, as the Board may specify. The Board may at any time accelerate the time at which the restrictions on all or any part of the shares shall lapse.

6.2.3 Rights as a Stockholder. A Participant who acquires shares of restricted stock will have all of the rights of a Stockholder with respect to such shares including the right to receive dividends and to vote such shares. Unless the Board otherwise determines, certificates evidencing shares of restricted stock will remain in the possession of the Company until such shares are free of all restrictions under the Plan.

6.2.4 Purchase Price. The purchase price of shares of restricted stock shall be determined by the Board, in its sole discretion.

6.2.5 Other Awards Settled With Restricted Stock. The Board may provide that any or all the Common Stock delivered pursuant to an Award will be restricted stock.

6.2.6 Unrestricted Stock. The Board may, in its sole discretion, sell to any Participant shares of Common Stock free of restrictions under the Plan for a price determined by the Board, but which may not be less than the par value per share of the Common Stock.

6.3 Deferred Stock

6.3.1 Deferred Stock Award. A deferred stock Award entitles the recipient to receive shares of deferred stock, which is Common Stock to be delivered in the future. Delivery of the Common Stock will take place at such time or times, and on such conditions, as the Board may specify. The Board may at any time accelerate the time at which delivery of all or any part of the Common Stock will take place.

6.3.2 Other Awards Settled with Deferred Stock. The Board may, at the time any Award described in this Section 6 is granted, provide that, at the time Common Stock would otherwise be delivered pursuant to the Award, the Participant will instead receive an instrument evidencing the right to future delivery of deferred stock.

6.4 Performance Awards

6.4.1 Performance Awards. A performance Award entitles the recipient to receive, without payment, an amount, in cash or Common Stock or a combination thereof (such form to be determined by the Board), following the attainment of performance goals. Performance goals may be related to personal performance, corporate performance, departmental performance or any other category of performance deemed by the Board to be important to the success of the Company. The Board will determine the performance goals, the period or periods during which performance is to be measured and all other terms and conditions applicable to the Award.

6.4.2 Other Awards Subject to Performance Conditions. The Board may, at the time any Award described in this Section 6 is granted, impose a condition or conditions (in addition to any conditions specified or authorized in this Section 6 of the Plan) that performance goals be met prior to the Participant's realization of any payment or benefit under the Award.

7. Purchase Price and Payment

Except as otherwise provided in the Plan, the purchase price of Common Stock to be acquired pursuant to an Award shall be the price determined by the Board, provided that such price shall not be less than the par value of the Common Stock. Except as otherwise provided in the Plan, the Board may determine the method of payment of the exercise price or purchase price of an Award granted under the Plan and the form of payment. The Board may determine that all or any part of the purchase price of Common Stock pursuant to an Award has been satisfied by past services rendered by the Participant. The Board may agree at any time, upon request of the Participant, to defer the date on which any payment under an Award will be made.

8. Loans and Supplemental Grants

The Company may make a loan to a Participant, either on or after the grant to the Participant of any Award, in connection with the purchase of Common Stock under the Award or with the payment of any obligation incurred or recognized as a result of the Award. The Board will have full authority to decide whether the loan is to be secured or unsecured or with or without recourse against the borrower, the terms on which the loan is to be repaid and the conditions, if any, under which it may be forgiven.

In connection with any Award, the Board may at the time such Award is made or at a later date, provide for and make a cash payment to the participant not to exceed an amount equal to (a) the amount of any federal, state and local income tax or ordinary income for which the Participant will be liable with respect to the Award, plus (b) an additional amount on a grossed-up basis necessary to make him or her whole after tax, discharging all the participant's income tax liabilities arising from all payments under the Plan.

9. Change in Control

9.1 Impact of Event

In the event of a "Change in Control" as defined in Section 9.2, as applicable, the following provisions shall apply, unless the agreement evidencing the Award otherwise provides (by specific explicit reference to Section 9.2 below). If a Change in Control occurs while any Awards are outstanding, then, effective upon the Change in Control, (i) each outstanding stock option or other stock-based Award awarded under the Plan that was not previously exercisable and vested shall become immediately exercisable in full and vested, and will no longer be subject to a right of repurchase by the Company, (ii) each outstanding restricted stock award or other stock-based Award subject to restrictions and to the extent not fully vested, shall be deemed to be fully vested, free of restrictions and conditions and no longer subject to a right of repurchase by the Company, and (iii) deferral limitations and conditions that relate solely to the passage of time, continued employment or affiliation will be waived and removed as to deferred stock Awards and performance Awards; performance of other conditions (other than conditions relating solely to the passage of time, continued employment or affiliation) will continue to apply unless otherwise provided in the agreement evidencing the Award or in any other agreement between the Participant and the Company or unless otherwise agreed by the Board.

9.2 Definition of "Change in Control"

"Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Person") of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 40% or more of either (i) the then-outstanding shares of common stock of the Company (the "Outstanding Common Stock") or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the "Outstanding Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions of shares of Common Stock shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the board of directors of a successor corporation to the Company), where the term "Continuing Director" means at any date a member of the Board (i) who was a member of the Board as of December 10, 2001 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a "Business Combination"), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Common Stock and Outstanding Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 60% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company's assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the "Acquiring Corporation") in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Common Stock and Outstanding Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 40% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

10. General Provisions

10.1 Documentation of Awards

Awards will be evidenced by written instruments, which may differ among Participants, prescribed by the Board from time to time. Such instruments may be in the form of agreements to be executed by both the Participant and the Company or certificates, letters or similar instruments which need not be executed by the participant but acceptance of which will evidence agreement to the terms thereof. Such instruments shall conform to the requirements of the Plan and may contain such other provisions (including provisions relating to events of merger, consolidation, dissolution and liquidations, change of control and restrictions affecting either the agreement or the Common Stock issued thereunder), as the Board deems advisable.

10.2 Rights as a Stockholder

Except as specifically provided by the Plan or the instrument evidencing the Award, the receipt of an Award will not give a Participant rights as a Stockholder with respect to any shares covered by an Award until the date of issue of a stock certificate to the participant for such shares.

10.3 Conditions on Delivery of Stock

The Company will not be obligated to deliver any shares of Common Stock pursuant to the Plan or to remove any restriction from shares previously delivered under the Plan (a) until all conditions of the Award have been satisfied or removed, (b) until, in the opinion of the Company's counsel, all applicable federal and state laws and regulations have been complied with, (c) if the outstanding Common Stock is at the time listed on any stock exchange, until the shares have been listed or authorized to be listed on such exchange upon official notice of issuance, and (d) until all other legal matters in connection with the issuance and delivery of such shares have been approved by the Company's counsel. If the sale of Common Stock has not been registered under the Securities Act of 1933, as amended, the Company may require, as a condition to exercise of the Award, such representations or agreements as counsel for the Company may consider appropriate to avoid violation of such act and may require that the certificates evidencing such Common Stock bear an appropriate legend restricting transfer.

If an Award is exercised by the participant's legal representative, the Company will be under no obligation to deliver Common Stock pursuant to such exercise until the Company is satisfied as to the authority of such representative.

10.4 Tax Withholding

The Company will withhold from any cash payment made pursuant to an Award an amount sufficient to satisfy all federal, state and local withholding tax requirements (the "withholding requirements").

In the case of an Award pursuant to which Common Stock may be delivered, the Board will have the right to require that the participant or other appropriate person remit to the Company an amount sufficient to satisfy the withholding requirements, or make other arrangements satisfactory to the Board with regard to such requirements, prior to the delivery of any Common Stock. If and to the extent that such withholding is required, the Board may permit the participant or such other person to elect at such time and in such manner as the Board provides to have the Company hold back from the shares to be delivered, or to deliver to the Company, Common Stock having a value calculated to satisfy the withholding requirement.

10.5 Transferability of Awards

Except as may be authorized by the Board, in its sole discretion, no Award (other than an Award in the form of an outright transfer of cash or Common Stock not subject to any restrictions) may be sold, assigned, transferred, pledged or otherwise encumbered other than by will or the laws of descent and distribution, and during a Participant's lifetime an Award requiring exercise may be exercised only by him or her (or in the event of incapacity, the person or persons properly appointed to act on his or her behalf). The Board may, in its discretion, determine the extent to which Awards granted to a Participant shall be transferable, and such provisions permitting or acknowledging transfer shall be set forth in the written agreement evidencing the Award executed and delivered by or on behalf of the Company and the Participant.

10.6 Adjustments in the Event of Certain Transactions

(a) In the event of a stock dividend, stock split or combination of shares, or other distribution with respect to holders of Common Stock other than normal cash dividends, the Board will make (i) appropriate adjustments to the maximum number of shares that may be delivered under the Plan under Section 4 above and (ii) appropriate adjustments to the number and kind of shares of stock or securities subject to Awards then outstanding or subsequently granted, any exercise prices relating to Awards and any other provisions of Awards affected by such change.

(b) In the event of any recapitalization, merger or consolidation involving the Company, any transaction in which the Company becomes a subsidiary of another entity, any sale or other disposition of all or a substantial portion of the assets of the Company or any similar transaction, as determined by the Board, the Board in its discretion may make appropriate adjustments to outstanding Awards to avoid distortion in the operation of the Plan.

10.7 Employment Rights

Neither the adoption of the Plan nor the grant of Awards will confer upon any person any right to continued employment with the Company or any subsidiary or interfere in any way with the right of the Company or subsidiary to terminate any employment relationship at any time or to increase or decrease the compensation of such person. Except as specifically provided by the Board in any particular case, the loss of existing or potential profit in Awards granted under the Plan will not constitute an element of damages in the event of termination of an employment relationship even if the termination is in violation of an obligation of the Company to the employee.

Whether an authorized leave of absence, or absence in military or government service, shall constitute termination of employment shall be determined by the Board at the time. For purposes of this Plan, transfer of employment between the Company and its subsidiaries shall not be deemed termination of employment.

10.8 Other Employee Benefits

The value of an Award granted to a Participant who is an employee, and the amount of any compensation deemed to be received by an employee as a result of any exercise or purchase of Common Stock pursuant to an Award or sale of shares received under the Plan, will not constitute “earnings” or “compensation” with respect to which any other employee benefits of such employee are determined, including without limitation benefits under any pension, stock ownership, stock purchase, life insurance, medical, health, disability or salary continuation plan.

10.9 Legal Holidays

If any day on or before which action under the Plan must be taken falls on a Saturday, Sunday or legal holiday, such action may be taken on the next succeeding day not a Saturday, Sunday or legal holiday.

10.10 Foreign Nationals

Without amending the Plan, Awards may be granted to persons who are foreign nationals or employed outside the United States or both, on such terms and conditions different from those specified in the Plan, as may, in the judgment of the Board, be necessary or desirable to further the purpose of the Plan.

10.11 Governing Law

The provisions of the Plan and all Awards made hereunder shall be governed by and interpreted in accordance with the laws of the State of Delaware, without regard to any applicable conflicts of law.

11. Termination and Amendment

The Plan shall remain in full force and effect until terminated by the Board. Subject to the last sentence of this Section 11, the Board may at any time or times amend the Plan or any outstanding Award for any purpose that may at the time be permitted by law, or may at any time terminate the Plan as to any further grants of Awards. No amendment of the Plan or any agreement evidencing Awards under the Plan may adversely affect the rights of any participant under any Award previously granted without such participant's consent.

12. Compliance with Section 409A of the Code

To the extent applicable to an Award, it is intended that this Plan and Awards made under the Plan comply with the provisions of Section 409A of the Code and applicable rules and regulations. The Plan and any Awards to which Section 409A is applicable will be administered in a manner consistent with this intent, and any provision that would cause this Plan or any Award made under the Plan to fail to satisfy Section 409A of the Code, to the extent applicable, shall have no force and effect until amended to comply with Section 409A of the Code (which amendment may be retroactive to the extent permitted by Section 409A and may be made by the Company without the consent of Participants to which Section 409A shall apply).

Except as provided in individual Award agreements initially or by amendment, if and to the extent any portion of any payment, compensation or other benefit provided to a Participant in connection with his or her employment termination is determined to constitute "nonqualified deferred compensation" within the meaning of Section 409A of the Code and the Participant is a specified employee as defined in Section 409A(a)(2)(B)(i) of the Code, as determined by the Company in accordance with its procedures, by which determination the Participant (through accepting the Award) agrees that he or she is bound, such portion of the payment, compensation or other benefit shall not be paid before the day that is six months plus one day after the date of "separation from service" (as determined under Code Section 409A) (the "***New Payment Date***"), except as Code Section 409A may then permit. The aggregate of any payments that otherwise would have been paid to the Participant during the period between the date of separation from service and the New Payment Date shall be paid to the Participant in a lump sum on such New Payment Date, and any remaining payments will be paid on their original schedule.

The Company makes no representations or warranty and shall have no liability to the Participant or any other person if any provisions of or payments, compensation or other benefits under the Plan are determined to constitute nonqualified deferred compensation subject to Section 409A of the Code but do not to satisfy the conditions of that section.

As amended effective December 9, 2008

Exhibit 10.7

KADANT INC.

2006 EQUITY INCENTIVE PLAN

1. Purpose

The purpose of this 2006 Equity Incentive Plan (the "Plan") of Kadant Inc. (the "Company") is to advance the interests of the Company and its stockholders by enhancing the Company's ability to attract, retain and motivate persons (such as employees, officers and directors of, and consultants to, the Company and its subsidiaries) who are expected to make significant contributions to the future growth and success of the Company and its subsidiaries. The Plan is intended to accomplish these goals by enabling the Company to offer such persons equity ownership opportunities or performance-based stock incentives in the Company, or any combination thereof ("Awards"), that are intended to align their interests with those of the Company's stockholders and to encourage them to continue in the service of the Company and to pursue the long-term growth, profitability and financial success of the Company.

2. Administration

The Plan will be administered by the Board of Directors of the Company (the "Board"). The Board shall have full power to interpret and administer the Plan, including full authority to:

- prescribe, amend and rescind rules and regulations relating to the Plan and Awards,
- select the persons to whom Awards will be granted ("Participants"),
- determine the type and amount of Awards to be granted to Participants (including any combination of Awards),
- determine the terms and conditions of Awards granted under the Plan (including terms and conditions relating to events of merger, consolidation, dissolution and liquidation, change in control, vesting, forfeiture, restrictions, dividends and interest, if any, on deferred amounts),
- waive compliance by a Participant with any obligation to be performed by him or her under an Award,
- waive any term or condition of an Award, cancel an existing Award in whole or in part with the consent of a Participant,
- grant replacement Awards,
- accelerate the vesting or lapse of any restrictions of any Award,
- correct any defect, supply any omission or reconcile any inconsistency in the Plan or in any Award, and
- adopt the form of instruments evidencing Awards under the Plan and change such forms from time to time.

Any interpretation by the Board of the terms and provisions of the Plan or any Award thereunder and the administration thereof, and all action taken by the Board, shall be final, binding and conclusive on all parties and any person claiming under or through any party. No director shall be liable for any action or determination made in good faith.

The Board may, to the full extent permitted by law, delegate any or all of its responsibilities under the Plan to a committee (the "Committee") appointed by the Board and consisting of independent members of the Board. All references in the Plan to the "Board" shall mean the Board or a Committee of the Board to the extent that the Board's powers or authority under the Plan have been delegated to such Committee.

3. Effective Date

The Plan was adopted by the Board on March 7, 2006, subject to the approval of the Plan by the Company's stockholders. No Awards may be granted under the Plan unless and until the Plan has been approved by the Company's stockholders and no Awards may be made under the Plan after the tenth anniversary of the date of such stockholder approval.

4. Shares Available for Awards

4.1 Authorized Number of Shares

Subject to adjustment as provided in Section 9.6, the total number of shares of common stock of the Company, par value $.01 per share (the "Common Stock"), reserved and available for distribution under the Plan shall be 900,000 shares. Such shares may consist, in whole or in part, of authorized and unissued shares or treasury shares.

4.2 Share Counting

The following rules shall apply in determining the number of shares of Common Stock remaining available for issuance under the Plan:

- shares of Common Stock covered by Awards of stand-alone stock appreciation rights shall be counted against the number of shares available for the grant of Awards under the Plan; provided that Awards of stand-alone stock appreciation rights that may be settled in cash only shall not be so counted;
- if any Award of shares of Common Stock expires or terminates without having been exercised in full, is forfeited or is otherwise terminated, surrendered or cancelled in whole or in part (including as a result of shares of Common Stock subject to such Award being repurchased by the Company pursuant to the terms of any Award, the unused shares of Common Stock covered by such Award shall be available again for the future grant of Awards under the Plan, subject, however, in the case of Incentive Stock Options (as hereinafter defined), to any applicable limitations under the Internal Revenue Code of 1986, as amended (the "Code");
- if any Award results in Common Stock not being issued (including as a result of an stand-alone stock appreciation right that could be settled either in cash or in stock and was actually settled in cash), the unused shares of Common Stock covered by such Award shall be available again for the future grant of Awards under the Plan, subject, however, in the case of Incentive Stock Options (as hereinafter defined), to any limitations under the Code;
- Shares of Common Stock tendered to the Company by a Participant to purchase

shares of Common Stock upon the exercise of an Award or to satisfy tax withholding obligations (including shares retained from the Award creating the tax obligation), the number of shares tendered shall be added to the number of shares of Common Stock available for the future grant of Awards under the Plan

- Any shares of Common Stock underlying Awards granted in assumption of, or in substitution for, outstanding awards previously granted by a company acquired by the Company or any of its subsidiaries or affiliates or with which the Company or any of its subsidiaries or affiliates combines, shall not, unless required by law or regulation, count against the number of shares of Common Stock available for the future grant of Awards under the Plan.

4.3 <u>Participant Limitation</u>

Subject to adjustment as provided in Section 9.6, the maximum number of shares of Common Stock permitted to be granted under any Award or combination of Awards to a single Participant during any one calendar year shall be 500,000 shares of Common Stock.

5. <u>Eligibility</u>

All of the employees, officers and directors of, and consultants to, the Company and its subsidiaries, or other persons are eligible to receive Awards under the Plan. The Board, or other appropriate committee or person to the extent permitted pursuant to the last two sentences of Section 2, shall from time to time select from among such eligible persons those who will receive Awards under the Plan.

6. <u>Types of Awards</u>

The Board may offer Awards under the Plan in any form of equity-based interest, equity-based incentive or performance-based stock incentive in Common Stock of the Company or any combination thereof. The type, terms and conditions and restrictions of an Award shall be determined by the Board at the time such Award is made to a Participant. An Award shall be made at the time specified by the Board, shall be subject to such conditions or restrictions as may be imposed by the Board and shall conform to the general rules applicable under the Plan as well as any special rules then applicable under federal tax laws or regulations or the federal securities laws relating to the type of Award granted.

Without limiting the foregoing, Awards may take the following forms and shall be subject to the following rules and conditions:

6.1 <u>Options</u>

An option is an Award that entitles the holder on exercise thereof to purchase Common Stock at a specified exercise price. Options granted under the Plan may be either incentive stock options (“incentive stock options”) that meet the requirements of Section 422 of the Code, or options that are not intended to meet the requirements of Section 422 of the Code (“nonstatutory options”).

6.1.1 Option Price. The price at which Common Stock may be purchased upon exercise of an option shall be determined by the Board, provided however, the exercise price shall not be less than 100% of the fair market value per share of Common Stock as determined by (or in a manner approved by) the Board as of the date of grant.

6.1.2 Option Grants. The granting of an option shall take place at the time specified by the Board. Options shall be evidenced by written option agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including but not limited to vesting and forfeiture provisions, acceleration, change in control, protection in the event of merger, consolidations, dissolutions and liquidations) as the Board shall deem advisable. Option agreements shall expressly state whether an option grant is intended to qualify as an incentive stock option or nonstatutory option.

6.1.3 Option Period. An option will become exercisable at such time or times (which may be immediately or in such installments as the Board shall determine) and on such terms and conditions as the Board shall specify. The option agreements shall specify the terms and conditions applicable in the event of an option holder's termination of employment during the option's term. No option may be granted for a term in excess of 10 years.

Any exercise of an option must be in writing, signed by the proper person and delivered or mailed to the Company, accompanied by (1) any additional documents required by the Board and (2) payment in full in accordance with Section 6.1.4 for the number of shares for which the option is exercised.

6.1.4 Payment of Exercise Price. Stock purchased on exercise of an option shall be paid for as follows: (1) in cash or by check (subject to such guidelines as the Company may establish for this purpose), bank draft or money order payable to the order of the Company or (2) if so permitted by the instrument evidencing the option (or in the case of a nonstatutory option, by the Board at or after grant of the option), (i) through the delivery of shares of Common Stock that have been outstanding for at least six months (or such other minimum length of time the Board expressly approves) and that have a fair market value (determined in accordance with procedures prescribed by the Board) equal to the exercise price, (ii) by delivery of a promissory note of the option holder to the Company, payable on such terms as are specified by the Board, (iii) by delivery of an unconditional and irrevocable undertaking by a broker to deliver promptly to the Company sufficient funds to pay the exercise price, (iv) by any combination of the foregoing permissible forms of payment or (v) such other lawful consideration as the Board may determine.

6.1.5 Limitation on Repricing. Unless approved by the Company's stockholders, No outstanding option granted under the Plan may be amended to provide an exercise price per share that is lower than the current exercise price per share of such outstanding option (other than adjustments pursuant to Section 9.6).

6.1.6 Special Rules for Incentive Stock Options. Each provision of the Plan and each option agreement evidencing an incentive stock option shall be construed so that each incentive stock option shall be an incentive stock option as defined in Section 422 of the Code or any statutory provision that may replace such Section, and any provisions thereof that cannot be so construed shall be disregarded. Instruments evidencing incentive stock options shall contain such provisions as are required under applicable provisions of the Code. Incentive stock options may be granted only to employees of the Company and its subsidiaries.

6.2 Stock Appreciation Rights

A stock appreciation right ("SAR") is an Award entitling the recipient, upon exercise, to receive an amount in cash or Common Stock or a combination thereof (in such form to be determined by the Board) determined in whole or in part by reference to appreciation after the date of grant in the fair market value of a share of Common Stock. The terms of SARs shall be determined by the Board in its discretion. SARs may be granted in tandem with, or separately from, Options granted under the Plan.

6.2.1 Tandem Awards. Participants may be granted a tandem SAR, consisting of SARs granted with an underlying option, exercisable upon such terms and conditions as the Board shall establish. Tandem SARs shall provide that the Participant may elect between the exercise of the underlying option for shares of Common Stock or the surrender of the option in exchange for a distribution from the Company in an amount equal to the excess of (a) the fair market value (on the option surrender date) of the number of shares in which the Participant is at the time vested under the surrendered option (or surrendered portion thereof) over (b) the aggregate exercise price payable for such vested shares. No option surrender shall be effective unless it is approved by the Board, either at the time of the actual option surrender or at any earlier time. If the option surrender is approved, then the distribution to the Participant may be made in shares valued at fair market value (on the option surrender date), in cash, or party in shares and partly in cash, as the Board shall deem appropriate. If the surrender of an option is not approved by the Board, then the Participant shall retain whatever rights he or she had under the surrendered option (or surrendered portion thereof) on the option surrender date and may exercise such rights in accordance with the terms of the option Award.

6.2.2 Stand-alone SARs. Participants may be granted a SAR not expressly granted in tandem with an option. The stand-alone SAR shall cover a specified number of shares of Common Stock and shall be exercisable upon such terms and conditions as the Board shall establish. will become exercisable at such time or times and on such conditions as the Board may specify in the SAR Award. Upon exercise of a stand-alone SAR, a Participant shall be entitled to receive a distribution from the Company in an amount equal to the excess of (a) the fair market value (on the exercise date) of the number of shares underlying the exercised right over (b) the aggregate base price in effect for those shares. The number of shares underlying each stand-alone SAR and the base price in effect for those shares shall be determined by the Board at the time the stand-alone SAR is granted, provided however, that the base price per share may not be less than the fair market value per underlying share on the date of grant. The distribution to the Participant with respect to an exercised stand-alone SAR may be made in shares valued at fair market value on the exercise date, in cash, or party in shares and partly in cash, as the Board shall deem appropriate.

6.2.3 Limitation on Repricing. Unless approved by the Company's stockholders, no outstanding SAR granted under the Plan may be amended to decrease the exercise price or base price applicable to such SAR (other than adjustments pursuant to Section 9.6).

6.3 Restricted Stock and Restricted Stock Units

An Award of restricted stock entitles the recipient thereof to acquire shares of Common Stock upon payment of the purchase price, if any, subject to restrictions specified in the instrument evidencing the Award. A restricted stock unit is an Award of a contractual right to receive, at a future date, shares or an amount based on the fair market value of a share of Common Stock, subject to restrictions specified in the instrument evidencing the Award.

6.3.1 Restricted Stock Awards. Awards of restricted stock and restricted stock units shall be evidenced by written agreements. Such agreements shall conform to the requirements of the Plan, and may contain such other provisions (including restriction and forfeiture provisions, restrictions based upon the achievement of specific performance goals, change in control, protection in the event of mergers, consolidations, dissolutions and liquidations) as the Board shall deem advisable. Restricted stock units awarded to a Participant may be settled in shares valued at fair market value on the settlement date, in cash, or partly in shares or partly in cash, as the Board shall deem appropriate.

6.3.2 Restrictions. Until the restrictions specified in a restricted stock agreement shall lapse, restricted stock may not be sold, assigned, transferred, pledged or otherwise encumbered or disposed of, and upon certain conditions specified in the restricted stock agreement, must be resold to the Company for the price, if any, specified in such agreement. The restrictions shall lapse at such time or times, and on such conditions, as the Board may specify. The Board may at any time accelerate the time at which the restrictions on all or any part of the shares shall lapse.

6.3.3 Vesting. Awards of restricted stock or restricted stock units that vest based on the passage of time alone shall be vest ratably on each of the first three anniversaries of the date of grant ($^1/_3$ on the first anniversary, an additional $^1/_3$ on the second anniversary and 100% on the third anniversary). This vesting provision shall not apply to Awards that vest based on performance goals determined by the Board (including performance-based compensation Awards under Section 6.4). In addition, the Board may grant up to a maximum of 250,000 shares of Common Stock with vesting provisions that vary from the first sentence of this Section 6.3.3.

6.3.4 Rights as a Stockholder. A Participant holding an Award of restricted stock units shall have no ownership interest in the shares of Common Stock to which the restricted stock units relate until payment with respect to such restricted stock units is actually made in shares of Common Stock. A Participant who acquires shares of restricted stock will have all of the rights of a Stockholder with respect to such shares including the right to receive dividends and to vote such shares, although the Board may determine that dividends and other property payable to a Participant shall be distributed only if and when the restrictions imposed on the applicable restricted stock lapse. Unless the Board otherwise determines, certificates evidencing shares of restricted stock will remain in the possession of the Company until such shares are free of all restrictions under the Plan.

6.3.5 Purchase Price. The purchase price of shares of restricted stock shall be determined by the Board, in its sole discretion.

6.3.6 Other Awards Settled With Restricted Stock. The Board may provide that any or all of the Common Stock delivered pursuant to an Award will be restricted stock.

6.4 Performance-Based Compensation

6.4.1 Performance Awards. A performance Award entitles the recipient to receive, without payment, an amount, in cash or Common Stock or a combination thereof (such form to be determined by the Board), following the attainment of performance goals. Performance goals may be related to personal performance, corporate performance, departmental performance or any other category of performance deemed by the Board to be important to the success of the Company. The Board will determine the performance goals, the period or periods during which performance is to be measured and all other terms and conditions applicable to the Award.

6.4.2 Section 162(m) Performance-Based Awards. The Board may delegate the administration and grant of Awards to a Committee approved by the Board, the members of which all are “outside directors” as defined by Section 162(m) (the “Section 162(m) Committee”), for the purpose of granting Awards that satisfy all the requirements for “performance-based compensation” within the meaning of Section 162(m)(4)(C) of the Code (“Performance-based Compensation”). If the Section 162(m) Committee determines, at the time a restricted stock Award or other stock-based Award is granted to a Participant, that such Participant is, or is likely to be as of the end of the tax year in which the Company would claim a tax deduction in connection with such Award, a “Covered Employee” (as defined in Section 162(m)), then the Section 162(m) Committee may provide that this Section 6.4.2 is applicable to such Award. The Section 162(m) Committee may be the same as the Compensation Committee, if the members of the Compensation Committee meet the criteria for the Section 162(m) Committee.

6.4.2.1 Performance Measures. Awards subject to this Section shall provide that the lapsing of restriction and the distribution of cash or shares pursuant to the Award, as applicable, shall be subject to the achievement of one or more objective performance goals established by the Section 162(m) Committee, which shall be based on attainment of specified levels of one or any combination of the following, which may be absolute in their terms or measured against or in relationship to other companies comparably, similarly or otherwise situated, (collectively “Performance Measures”): (a) earnings per share, (b) return on average equity or average assets in relation to a peer group of companies designated by the Section 162(m) Committee, (c) earnings, (d) earnings growth, (e) earnings per share growth, (f) earnings before interest, taxes and amortization (“EBITA”), (g) earnings before interest, taxes, depreciation and amortization (“EBITDA”), (h) operating income, (i) operating margins, (j) division income, (k) revenues, (l) expenses, (m) stock price, (n) market share, (o) return on sales, assets, equity or investment, (p) achievement of balance sheet or income statement objectives, (q) net cash provided from continuing operations, (r) stock price appreciation, (s) total shareholder return, (t) strategic initiatives, (u) cost control, (v) net operating profit after tax, (w) pre-tax or after-tax income, (x) cash flow, (y) net income, and (z) financial ratios contained in the Company's debt instruments. To the extent not inconsistent under Section 162(m), the measurement of Performance Measures may exclude or be adjusted to reflect any one or more of (i) extraordinary items or other unusual or non-recurring items, (ii) discontinued operations, (iii) gains or losses on the dispositions of discontinued operations, (iv) cumulative effects of changes in accounting principles, (v) the writedown of any asset and (vi) charges for restructuring and rationalization programs. The Performance Measures may be particular to a Participant, or the department, branch, line of business, subsidiary or other unit in which the Participant works and may cover such period as may be specified by the Section 162(m) Committee. Performance Measures will be set by the Section 162(m) Committee within the time period prescribed by, and shall otherwise comply with the requirements of, Section 162(m).

6.4.2.2 **Adjustment of Performance Measures**. With respect to Awards that are intended to be subject to this Section 6.4.2, the Section 162(m) Committee may adjust downwards, but not upwards, the cash or number of Shares payable pursuant to such Award, and the Section 162(m) Committee may not waive the achievement of the applicable performance goals except in the case of the death or disability of the Participant.

6.4.2.3 **Committee Discretion**. Nothing in this Section 6.4.2 is intended to limit the Board's discretion to adopt conditions or goals that relate to performance with respect to any Award that is not intended to qualify as Performance-based Compensation. In addition, the Board may, subject to the terms of the Plan, amend previously granted Award in a way that disqualifies them as Performance-based Compensation.

6.4.2.4 **Change in Law**. In the event that the requirements of Section 162(m) and the regulations thereunder change to permit the Section 162(m) Committee discretion to alter the Performance Measures without obtaining stockholder approval of such changes, the Section 162(m) Committee shall have sole discretion to make such changes without obtaining stockholder approval.

6.5 Other Stock-Based Awards

The Board may grant equity-based or equity-related Awards not otherwise described herein in such amounts and subject to such terms and conditions as the Board may determine. By way of illustration and not limitation, such other stock-based Awards may (i) involve the transfer of actual shares of Common Stock, either at the time of grant or thereafter, or payment in cash or otherwise of amounts based on the value of shares of Common Stock; (ii) be subject to performance-based or service-based conditions; (iii) be in the form of phantom stock, restricted stock, restricted stock units, performance shares or other form of stock-based incentive; or (iv) be designed to comply with applicable laws of jurisdictions other than the United States.

6.6 Deferred Payments or Delivery of Shares; Limitation on Options and SARs

The Board may determine that all or a portion of any Award to a Participant, whether it is to be paid in cash, shares of Common Stock or a combination, shall be deferred or may, in its sole discretion, approve deferral elections by Participants, on such conditions, as the Board may specify. The Board may at any time accelerate the time at which delivery of all or any part of shares of the Common Stock will take place. Notwithstanding the foregoing, deferral of option or SAR gains shall not be permitted under the Plan.

7. **Purchase Price and Payment**

Except as otherwise provided in the Plan, the purchase price of Common Stock to be acquired pursuant to an Award shall be the price determined by the Board, provided that such price shall not be less than the par value of the Common Stock. Except as otherwise provided in the Plan, the Board may determine the method of payment of the exercise price or purchase price of an Award granted under the Plan and the form of payment. The Board may determine that all or any part of the purchase price of Common Stock pursuant to an Award has been satisfied by past services rendered by the Participant. The Board may agree at any time, upon request of the Participant, to defer the date on which any payment under an Award will be made.

8. **Change in Control**

8.1 Impact of Event

In the event of a "Change in Control" as defined in Section 8.2, as applicable, the following provisions shall apply, unless the agreement evidencing the Award otherwise provides (by specific explicit reference to Section 8.2 below). If a Change in Control occurs while any Awards are outstanding, then, effective upon the Change in Control, all outstanding Awards of a Participant shall be accelerated as follows: (i) each outstanding stock option, stock appreciation right or other stock-based Award granted under the Plan that was not previously exercisable and vested shall become immediately exercisable in full and vested, and will no longer be subject to a right of repurchase by the Company, and will remain exercisable throughout their entire term, (ii) each outstanding restricted stock award, restricted stock unit or other stock-based Award subject to restrictions and to the extent not fully vested, shall be deemed to be fully vested, free of restrictions and conditions and no longer subject to a right of repurchase by the Company, and (iii) the restrictions and other deferral limitations applicable to other Awards shall lapse, and such other Awards shall become free of all restrictions, limitations or conditions and become fully vested and exercisable to the full extent of the original grant.

8.2 Definition of "Change in Control"

"Change in Control" means an event or occurrence set forth in any one or more of subsections (a) through (d) below (including an event or occurrence that constitutes a Change in Control under one of such subsections but is specifically exempted from another such subsection):

(a) the acquisition by an individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Person") of beneficial ownership of any capital stock of the Company if, after such acquisition, such Person beneficially owns (within the meaning of Rule 13d-3 promulgated under the Exchange Act) 20% or more of either (i) the then-outstanding shares of common stock of the Company (the "Outstanding Common Stock") or (ii) the combined voting power of the then-outstanding securities of the Company entitled to vote generally in the election of directors (the "Outstanding Voting Securities"); provided, however, that for purposes of this subsection (a), the following acquisitions of shares of Common Stock shall not constitute a Change in Control: (i) any acquisition by the Company, (ii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (iii) any acquisition by any corporation pursuant to a transaction which complies with clauses (i) and (ii) of subsection (c) of this definition; or

(b) such time as the Continuing Directors (as defined below) do not constitute a majority of the Board (or, if applicable, the board of directors of a successor corporation to the Company), where the term "Continuing Director" means at any date a member of the Board (i) who was a member of the Board as of March 8, 2006 or (ii) who was nominated or elected subsequent to such date by at least a majority of the directors who were Continuing Directors at the time of such nomination or election or whose election to the Board was recommended or endorsed by at least a majority of the directors who were Continuing Directors at the time of such nomination or election; provided, however, that there shall be excluded from this clause (ii) any individual whose initial assumption of office occurred as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents, by or on behalf of a person other than the Board; or

(c) the consummation of a merger, consolidation, reorganization, recapitalization or statutory share exchange involving the Company or a sale or other disposition of all or substantially all of the assets of the Company in one or a series of transactions (a "Business Combination"), unless, immediately following such Business Combination, each of the following two conditions is satisfied: (i) all or substantially all of the individuals and entities who were the beneficial owners of the Outstanding Common Stock and Outstanding Voting Securities immediately prior to such Business Combination beneficially own, directly or indirectly, more than 80% of the then-outstanding shares of common stock and the combined voting power of the then-outstanding securities entitled to vote generally in the election of directors, respectively, of the resulting or acquiring corporation in such Business Combination (which shall include, without limitation, a corporation which as a result of such transaction owns the Company or substantially all of the Company's assets either directly or through one or more subsidiaries) (such resulting or acquiring corporation is referred to herein as the "Acquiring Corporation") in substantially the same proportions as their ownership, immediately prior to such Business Combination, of the Outstanding Common Stock and Outstanding Voting Securities, respectively; and (ii) no Person (excluding the Acquiring Corporation or any employee benefit plan (or related trust) maintained or sponsored by the Company or by the Acquiring Corporation) beneficially owns, directly or indirectly, 20% or more of the then outstanding shares of common stock of the Acquiring Corporation, or of the combined voting power of the then-outstanding securities of such corporation entitled to vote generally in the election of directors; or

(d) approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

9. General Provisions

9.1 Documentation of Awards

Awards will be evidenced by written instruments, which may differ among Participants, prescribed by the Board from time to time. Such instruments may be in the form of agreements to be executed by both the Participant and the Company or certificates, letters or similar instruments which need not be executed by the participant but acceptance of which will evidence agreement to the terms thereof. Such instruments shall conform to the requirements of the Plan and may contain such other provisions (including provisions relating to events of merger, consolidation, dissolution and liquidations, change in control and restrictions affecting either the agreement or the Common Stock issued thereunder), as the Board deems advisable.

9.2 Rights as a Stockholder

Except as specifically provided by the Plan or the instrument evidencing the Award, the receipt of an Award will not give a Participant rights as a Stockholder with respect to any shares covered by an Award until the date of issue of a stock certificate to the Participant for such shares.

9.3 Conditions on Delivery of Stock

The Company will not be obligated to deliver any shares of Common Stock pursuant to the Plan or to remove any restriction from shares previously delivered under the Plan (a) until all conditions of the Award have been satisfied or removed, (b) until, in the opinion of the Company's counsel, all applicable federal and state laws and regulations have been complied with, (c) if the outstanding Common Stock is at the time listed on any stock exchange, until the shares have been listed or authorized to be listed on such exchange upon official notice of issuance, and (d) until all other legal matters in connection with the issuance and delivery of such shares have been approved by the Company's counsel. If the sale of Common Stock has not been registered under the Securities Act of 1933, as amended, the Company may require, as a condition to exercise of the Award, such representations or agreements as counsel for the Company may consider appropriate to avoid violation of such Act and may require that the certificates evidencing such Common Stock bear an appropriate legend restricting transfer.

If an Award is exercised by the Participant's legal representative, the Company will be under no obligation to deliver Common Stock pursuant to such exercise until the Company is satisfied as to the authority of such representative.

9.4 Tax Withholding

The Company will withhold from any cash payment made pursuant to an Award an amount sufficient to satisfy all federal, state and local withholding tax requirements (the "withholding requirements").

In the case of an Award pursuant to which Common Stock may be delivered, the Board will have the right to require that the Participant or other appropriate person remit to the

Company an amount sufficient to satisfy the withholding requirements, or make other arrangements satisfactory to the Board with regard to such requirements, prior to the delivery of any Common Stock. If and to the extent that such withholding is required, the Board may permit the Participant or such other person to elect at such time and in such manner as the Board provides to have the Company hold back from the shares to be delivered, or to deliver to the Company, Common Stock having a value calculated to satisfy the withholding requirement.

9.5 Transferability of Awards

Except as may be authorized by the Board, in its sole discretion, no Award (other than an Award in the form of an outright transfer of cash or Common Stock not subject to any restrictions) may be sold, assigned, transferred, pledged or otherwise encumbered other than by will or the laws of descent and distribution, and during a Participant's lifetime an Award requiring exercise may be exercised only by him or her (or in the event of incapacity, the person or persons properly appointed to act on his or her behalf). The Board may, in its discretion, permit or provide in an Award for the gratuitous transfer of the Award by the Participant to or for the benefit of any immediate family member, family trust or family partnership established solely for the benefit of the Participant and /or an immediate family member if, with respect to such proposed transferee, the Company would be eligible to use a Form S-8 for the registration of the sale of the Common Stock subject to such Award under the Securities Act of 1933, as amended, and provided that the Company shall not be required to recognize any such transfer until such time as the Participant and such permitted transferee shall, as a condition to such transfer, deliver to the Company a written instrument in form and substance satisfactory to the Company confirming that such transferee shall be bound by all of the terms and conditions of the Award.

9.6 Adjustments in the Event of Certain Transactions

(a) In the event of a stock dividend, stock split or combination of shares, or other distribution with respect to holders of Common Stock other than normal cash dividends, the Board will make (i) appropriate adjustments to the maximum number of shares that may be delivered under the Plan under Section 4 above and the participant limit set forth in Section 4, and (ii) appropriate adjustments to the number and kind of shares of stock or securities subject to Awards then outstanding or subsequently granted, any exercise prices relating to Awards and any other provisions of Awards affected by such change.

(b) In the event of any recapitalization, spinoff, merger or consolidation involving the Company, any transaction in which the Company becomes a subsidiary of another entity, any sale or other disposition of all or a substantial portion of the assets of the Company or any similar transaction, as determined by the Board, the Board in its discretion may make appropriate adjustments to outstanding Awards to avoid distortion in the operation of the Plan.

9.7 Employment Rights

Neither the adoption of the Plan nor the grant of Awards will confer upon any person any right to continued employment with the Company or any subsidiary or interfere in any way with the right of the Company or subsidiary to terminate any employment relationship at any time or to increase or decrease the compensation of such person. Except as specifically provided by the Board in any particular case, the loss of existing or potential profit in Awards granted under the Plan will not constitute an element of damages in the event of termination of an employment relationship even if the termination is in violation of an obligation of the Company to the employee.

Whether an authorized leave of absence, or absence in military or government service, shall constitute termination of employment shall be determined by the Board at the time. For purposes of this Plan, transfer of employment between the Company and its subsidiaries shall not be deemed termination of employment.

9.8 Other Employee Benefits

The value of an Award granted to a Participant who is an employee, and the amount of any compensation deemed to be received by an employee as a result of any exercise or purchase of Common Stock pursuant to an Award or sale of shares received under the Plan, will not constitute "earnings" or "compensation" with respect to which any other employee benefits of such employee are determined, including without limitation benefits under any pension, stock ownership, stock purchase, life insurance, medical, health, disability or salary continuation plan.

9.9 Legal Holidays

If any day on or before which action under the Plan must be taken falls on a Saturday, Sunday or legal holiday, such action may be taken on the next succeeding day not a Saturday, Sunday or legal holiday.

9.10 Foreign Nationals

Without amending the Plan, Awards may be granted to persons who are foreign nationals or employed outside the United States or both, on such terms and conditions different from those specified in the Plan, as may, in the judgment of the Board, be necessary or desirable to further the purpose of the Plan.

9.11 Governing Law

The provisions of the Plan and all Awards made hereunder shall be governed by and interpreted in accordance with the laws of the State of Delaware, without regard to any applicable conflicts of law.

9.12 Compliance with Section 409A of the Code

To the extent applicable to an Award, it is intended that this Plan and Awards made under the Plan comply with the provisions of Section 409A of the Code and applicable rules and regulations. The Plan and any Awards to which Section 409A is applicable will be administered in a manner consistent with this intent, and any provision that would cause this Plan or any

Award made under the Plan to fail to satisfy Section 409A of the Code, to the extent applicable, shall have no force and effect until amended to comply with Section 409A of the Code (which amendment may be retroactive to the extent permitted by Section 409A and may be made by the Company without the consent of Participants to which Section 409A shall apply).

Except as provided in individual Award agreements initially or by amendment, if and to the extent any portion of any payment, compensation or other benefit provided to a Participant in connection with his or her employment termination is determined to constitute “nonqualified deferred compensation” within the meaning of Section 409A of the Code and the Participant is a specified employee as defined in Section 409A(a)(2)(B)(i) of the Code, as determined by the Company in accordance with its procedures, by which determination the Participant (through accepting the Award) agrees that he or she is bound, such portion of the payment, compensation or other benefit shall not be paid before the day that is six months plus one day after the date of “separation from service” (as determined under Code Section 409A) (the “***New Payment Date***”), except as Code Section 409A may then permit. The aggregate of any payments that otherwise would have been paid to the Participant during the period between the date of separation from service and the New Payment Date shall be paid to the Participant in a lump sum on such New Payment Date, and any remaining payments will be paid on their original schedule.

The Company makes no representations or warranty and shall have no liability to the Participant or any other person if any provisions of or payments, compensation or other benefits under the Plan are determined to constitute nonqualified deferred compensation subject to Section 409A of the Code but do not to satisfy the conditions of that section.

10. **Termination and Amendment**

The Plan shall remain in full force and effect until terminated by the Board. Subject to the last sentence of this Section 10, the Board may at any time or times amend the Plan or any outstanding Award for any purpose that may at the time be permitted by law, or may at any time terminate the Plan as to any further grants of Awards. Notwithstanding the foregoing, (i) no amendment that would require stockholder approval under the rules of the New York Stock Exchange may be made effective until stockholder approval has been obtained, (ii) no amendment limiting or removing the prohibition on repricing of options shall be effective unless stockholder approval is obtained, (iii) to the extent required by Section 162(m) of the Code, no amendment applicable to an Award that is intended to comply with Section 162(m) shall be effective unless stockholder approval is obtained as required under Section 162(m) and (iv) to the extent required under Section 422 of the Code, no amendment or modification to an incentive stock option shall be effective unless stockholder approval is obtained. No amendment of the Plan or any agreement evidencing Awards under the Plan may materially adversely affect the rights of any Participant under any Award previously granted without such Participant’s consent.

As amended and in effect 12/09/08

Exhibit 10.10

KADANT INC.

CASH INCENTIVE PLAN

(Effective beginning with the 2007 Fiscal Year)

1. Purposes

The purposes of the Cash Incentive Plan of Kadant Inc. are (i) to enable the Company to attract, retain, motivate and reward employees by providing an opportunity to earn incentive compensation under the Plan related to the performance of the Company and its subsidiaries and (ii) to qualify such compensation paid as performance-based compensation within the meaning of Section 162(m) of the Code, as required for employees subject to Section 162(m) of the Code.

2. Definitions

Terms used in the Plan, and not otherwise defined, are defined as follows:

"Award" means a contingent award made to a Participant in accordance with the Plan that provides the Participant with the opportunity to earn cash compensation based on the relative level of attainment of Performance Goals established by the Committee for a Performance Period and on such other terms and conditions as the Committee shall determine.

"Board" means the Board of Directors of the Company.

"Code" means the U.S. Internal Revenue Code of 1986, as amended.

"Committee" means the Compensation Committee of the Board, or any other committee appointed by the Board to administer the Plan, so long as the committee is comprised of solely of two or more members of the Board who are "outside directors" within the meaning of Section 162(m).

"Company" means Kadant Inc., a Delaware corporation, or any successor to all or substantially all of the Company's business.

"Eligible Employee" means each executive officer, officer, or other key employee of the Company or any Subsidiary designated from time to time by the Committee as eligible to participate in the Plan.

"Participant" means any Eligible Employee who receives an Award under the Plan for a specified Performance Period.

"Performance Goals" means any one or a combination of the following: (i) earnings per share, (ii) return on average shareholders' equity or average assets, (iii) earnings, (iv) earnings or earnings per share growth, (v) earnings before interest, taxes and amortization (EBITA), (vi) earnings before interest, taxes, depreciation and amortization (EBITDA), (vii) operating income, (viii) operating margins, (ix) division income, (x) revenues, (xi) expenses, (xii) stock price, (xiii) market share, (xiv) return on sales, assets, equity, or investment, (xv) achievement of balance sheet or income statement objectives, (xvi) cash provided from operations, (xvii) stock price appreciation, (xviii) shareholder return, (xix) strategic initiatives, (xx) cost control, (xxi) net operating profit after tax, (xxii) pre-tax or after-tax income, (xxiii) cash flow, (xxiv) financial ratios contained in the Company's debt instruments, and (xxv) any other objective goals established by the Committee, with respect to Awards not required to qualify under Section 162(m).

"Performance Period" for an Award means the fiscal year of the Company, unless another period of time for the measurement of the extent to which the applicable Performance Goals are attained is designated by the Committee at the time the Award is made.

"Plan" means the Kadant Inc. Cash Incentive Plan, as amended from time to time.

"Section 162(m)" means Section 162(m) of the Code.

"Subsidiary" means (i) a corporation or other entity with respect to which the Company, directly or indirectly, has the power, whether through the ownership of voting securities, by contract or otherwise, to elect at least a majority of the members of such corporation's board of directors or analogous governing body or (ii) any other corporation or other entity in which the Company, directly or indirectly, has at least a majority equity or similar interest.

3. <u>Administration</u>

The Plan shall be administered by the Committee which shall have full power and authority, in its discretion, but subject to the express provisions of this Plan, to:

- select Participants from Eligible Employees;
- establish the terms and conditions of Awards, including the times at which Awards are made, the Performance Period to which an Award relates, and the Performance Goals to which an Award is subject;
- determine the extent to which cash payments are actually earned pursuant to Awards and the amounts to be paid;
- prescribe, amend and rescind rules and regulations relating to the Plan; and

- interpret this Plan and make all determinations necessary or advisable for the administration of the Plan.

The determinations of the Committee pursuant to its authority under the Plan shall be conclusive, final and binding. No member of the Committee shall be liable for any action or determination made in good faith with respect to the Plan or any Award.

4. <u>Eligibility</u>

Awards may be granted to any Eligible Employee.

5. <u>Awards</u>

The Committee shall, in its sole discretion, determine which Eligible Employees shall receive Awards and shall determine the Performance Period relating to each Award. For each Performance Period applicable to an Award, the Committee shall establish one or more Performance Goals, or any combination of Performance Goals, applicable to such Award and the other terms and conditions of the Award. Such Performance Goals and other terms and conditions shall be established by the Committee in its sole discretion as it shall deem appropriate and in the best interests of the Company and shall be established (i) within 90 days after the first day of the Performance Period and (ii) before 25% of the Performance Period has elapsed.

Performance Goals may take the form of absolute goals or goals relative to past performance of the Company or the current or past performance of one or more other companies comparable or similarly situated to the Company or of an index covering multiple companies. To the extent not inconsistent with qualification for an exemption from the deduction limit under Section 162(m), the Committee may specify that the Performance Goals exclude or be adjusted to reflect any one or more of (i) extraordinary items or other unusual or non-recurring items, (ii) discontinued operations, (iii) gains or losses on the dispositions of operations, (iv) effects of changes in accounting principles, (v) the write down of any asset or other impairment, (vi) the effect of foreign currency fluctuations, and (vii) charges for restructuring and rationalization programs. The Committee may establish Performance Goals that are particular to a Participant, or the department, branch, line of business, subsidiary, segment or other unit in which the Participant is employed or for which the Participant has supervisory responsibility and may cover such Performance Period as specified by the Committee.

After the end of each Performance Period for which the Committee has granted Awards, the Committee shall certify in writing the extent to which the Performance Goals established by the Committee for the Performance Period have been achieved and shall authorize the Company to make Award payments to Participants in accordance with the terms of the Awards. In no event shall the amount paid to a Participant in accordance with the terms of an Award by reason of Performance Goal achievement exceed $5,000,000 in any calendar year. Award payments shall be made to a Participant only upon the achievement of the applicable Performance Goals, except that the Committee may waive the achievement of Performance Goals in the event of the death, disability, a change in control of the Company or, for Awards not required to qualify under Section 162(m), such other event as the Committee may deem appropriate. Award payments to a Participant with respect to a Performance Period shall be made no later than the 15th day of the third month following the end of the taxable year of the Participant within which the last day of such Performance Period occurs.

The Committee may at any time, in its sole discretion, cancel an Award or eliminate or reduce (but not increase) the amount payable pursuant to the terms of an Award without the consent of a Participant.

The Committee shall have the power to impose such other restrictions on Awards as it may deem necessary or appropriate to ensure that such Awards satisfy all requirements for "performance-based compensation" within the meaning of Section 162(m)(4)(C), or any successor provision to such section of the Code.

6. Transferability

Awards shall not be subject to the claims of creditors and may not be assigned, alienated, transferred or encumbered in any way other than by will or the laws of descent and distribution.

7. Withholding Taxes

The Company may withhold or cause to be withheld from any and all cash payments made under this Plan such amounts as are necessary to satisfy all U.S. federal, state and local withholding tax requirements related to Awards or in accordance with the Company's payroll practices as from time to time in effect.

8. Amendment and Termination

The Committee may amend, modify or terminate the Plan in any respect at any time without the consent of Participants, provided that (i) no amendment or termination of the Plan may adversely affect any previously-granted Award without the consent of the affected Participant, except to the extent necessary to comply with Section 409A of the Code, and (ii) no amendment which would require shareholder approval under Section 162(m) may be effected without such shareholder approval.

9. Effective Date and Term of the Plan

This Plan shall be effective for the 2007 fiscal year of the Company, which begins December 31, 2006; provided however, that the Plan shall be void ab initio unless approved by a vote of the Company's Shareholders at the annual shareholders' meeting of the Company following adoption of the Plan by the Board and Committee.

Unless terminated earlier by action of the Board, the Plan shall expire on the date of the annual meeting of the Company's shareholders held in 2012, unless the Plan is extended and reapproved by a vote of the Company's shareholders at the annual shareholders' meeting held in 2012. Expiration of the Plan shall not affect any Awards outstanding on the date of the expiration and such Awards shall continue to be subject to the terms of the Plan, notwithstanding its termination. Upon expiration of the Plan, no further Awards may be granted under the Plan.

10. Miscellaneous

(a) No Rights to Awards or Employment. This Plan is not an employment contract between the Company and an Eligible Employee or Participant. No Eligible Employee shall have any claim or right to receive Awards under the Plan. Nothing in the Plan shall confer upon any employee of the Company any right to continued employment with the Company or any Subsidiary or interfere in any way with the right of the Company or a Subsidiary to terminate the employment of any of its employees at any time, with or without cause, including, without limitation, any individual who is then a Participant in the Plan.

(b) Other Compensation. Nothing in this Plan shall preclude or limit the ability of the Company to pay any compensation to a Participant under any other additional compensation and benefits plans, programs and arrangements, including, without limitation, any employee benefit plan, equity plan, or bonus plan, program or arrangement.

(c) Severability. If any provision of this Plan is held unenforceable, the remainder of the Plan shall continue in full force and effect without regard to such unenforceable provision and shall be applied as though the unenforceable provision were not included in the Plan. In addition, if any provision of this Plan would cause Awards not to constitute "qualified performance-based compensation" under Section 162(m), that provision shall be severed from, and shall be deemed not to be part of, the Plan, but the other provisions hereof shall remain in full force and effect. Any specific action by the Committee that would violate Section 162(m) and regulations thereunder shall be void.

(d) Governing Law. The Plan and all actions taken under the Plan shall be governed by and construed in accordance with the laws of the State of Delaware.

As amended and in effect 12/9/08

KADANT INC.
FORM OF FIRST AMENDMENT TO
PERFORMANCE-BASED RESTRICTED STOCK UNITS

Preamble. This amendment is effective as of December 9, 2008 with respect to the Performance-Based Restricted Stock Unit Award Agreements granted to the Recipient named below on the dates specified (the "Agreements"). This amendment is made by Kadant Inc. (the "Company") pursuant to the unilateral rights reserved under Section 7 of the Agreements to amend the Agreements to comply with Section 409A of the U.S. Internal Revenue Code.

Recipient: ________________________________

RSU Award Agreement dated: ______________

RSU Award Agreement dated: ______________

1. The last paragraph of Section 3 is hereby deleted and replaced in its entirety with the following paragraph (revised language appears in bold face):

> "As soon as administratively practicable after the Vesting Date, but in any event within the period ending on the later to occur of the date that is **2 1/2 months** from the end of the (i) Recipient's tax year that includes the Vesting Date, or (ii) the Company's fiscal year that includes the Vesting Date, the Company shall **cause** its transfer agent to issue **and deliver** the Award Shares in the name of the Recipient, subject to payment of all applicable withholding taxes pursuant to Section 6 below."

2. Section 4(b)(ii) is hereby amended by:

- deleting the words "deliver to" in the first sentence thereof and inserting the words "vest in" in replacement thereof;
- deleting the word "delivered" in the second sentence thereof and inserting the word "vested" in replacement thereof; and
- deleting the word "Delivered" in the second heading of the table and inserting the word "Vested" in replacement thereof.

3. Section 4(c) is hereby amended by:

- deleting the words " immediately issue" in the first sentence thereof and inserting the word "deliver as soon as administratively feasible but no later than 30 days after the Vesting Date" in replacement thereof; and
- deleting the words "immediately issue" in the second sentence thereof and inserting the words "deliver as soon as administratively feasible but no later than 30 days after the Vesting Date;

so that said Section 4(c) shall read in its entirety as follows:

"In the event of a "Change in Control" that occurs (i) prior to the Vesting Date and before the last day of the Measurement Period and (ii) on a date on which the Recipient is employed by the Company, then 100% of the Recipient's RSUs that have not previously been forfeited shall become immediately vested and shall no longer be subject to the Forfeiture provisions in this Section 4, and the Company shall deliver as soon as administratively feasible but no later than 30 days after the Vesting Date that number of Award Shares to the Recipient equal to the number shown on the first page of this Award Agreement, without adjustment. In the event of a "Change in Control that occurs (i) prior to the Vesting Date and on or after the last day of the Measurement Period and (ii) on a date on which the Recipient is employed by the Company, then 100% of the Recipient's RSUs that have not previously been forfeited shall become immediately vested and shall no longer be subject to the Forfeiture provisions in this Section 4, and the Company shall deliver as soon as administratively feasible but no later than 30 days after the Vesting Date that number of Award Shares to the Recipient equal to the number of Award Shares deliverable based on the achievement of the performance measures, as adjusted and determined in Section 3. A "Change in Control" shall have the same meaning for the purposes of this Award Agreement as set forth in Section 8 of the Plan, as the same may be amended from time to time."

4. The first sentence of Section 7 shall be amended by deleting the words "an elective" immediately prior to the words "deferral of compensation" and substituting the word "any" in replacement thereof, so that the first sentence shall read in its entirety as follows:

"Neither the Plan nor this Award Agreement is intended to provide for any deferral of compensation that would be subject to Section 409A ("Section 409A") of the U.S. Internal Revenue Code of 1986, as amended."

5. The last sentence of Section 7 shall be deleted and replaced in its entirety with the following sentence (revised language appears in bold face):

"Notwithstanding the provisions of Section 12(i), the Company reserves the right, to the extent the Company deems necessary or advisable in its sole discretion, to unilaterally amend or modify the Plan and/or this Award Agreement to ensure that **all** awards (including, without limitation the RSUs) **are either exempt from or compliant with** the requirements of Section 409A."

IN WITNESS WHEREOF, the undersigned has signed this First Amendment effective as of the 9th day of December, 2008, by order of the Board of Directors of Kadant Inc.

KADANT INC.

By: ______________________________

William A. Rainville
Chairman and Chief Executive Officer

Exhibit 10.16

FORM OF EXECUTIVE OFFICER PERFORMANCE-BASED RESTRICTED STOCK UNIT AWARD AGREEMENT

	Kadant Inc. ID: 52-1762325
Notice of Grant of Award **and Award Agreement**	One Technology Park Drive Westford, MA 01886

[Recipient name]	**Award Number:**	**[##]**
[Recipient address]	**Plan:**	**[##]**
	ID:	**[##]**

Effective [Date], you have been granted an award of [##] restricted stock units. These units are restricted until the vest date(s) shown below, at which time you will receive shares of Kadant Inc. (the Company) common stock.

The current total value of the award is $[##].

The award will vest in increments on the date(s) shown.

Shares	**Full Vest**
[##]	[Date]

By your signature and the Company's signature below, you and the Company agree that this award is granted under and governed by the terms and conditions of the Company's Award Plan as amended and the Award Agreement, all of which are attached and made a part of this document.

Kadant Inc.	Date
[Recipient name]	Date

KADANT INC.

AWARD AGREEMENT FOR
PERFORMANCE-BASED RESTRICTED STOCK UNITS
(“Award Agreement”)

1. **Preamble.** On the effective date shown on the first page of this Award Agreement (“Award Date”), the Company granted to the Recipient restricted stock units (“RSUs”) with respect to the number of shares of common stock of the Company identified on the first page of this Award Agreement (“Award Shares”), subject to the terms, conditions and restrictions set forth in this Award Agreement and the provisions of the Company’s 2006 Equity Incentive Plan (“Plan”). The RSUs represent a promise by the Company to deliver the Award Shares upon vesting. Any consideration due to the Company on the issuance of Award Shares pursuant to this Award Agreement will be deemed to have been satisfied by services rendered by the Recipient to the Company during the vesting period.

2. **Restrictions on Transfer.** Unless and until the Award Shares shall have vested as provided in Section 3 below, the Recipient shall not sell, transfer, pledge, hypothecate, assign or otherwise dispose of, by operation of law or otherwise, any RSUs, or any interest therein.

3. **Vesting Date.** Subject to the terms, conditions and restrictions of this Award Agreement, including the Forfeiture provisions described in Section 4 below, the Recipient shall vest in all RSUs on the last day of the Company’s [year] fiscal year, [Date] (the “Vesting Date”), provided that the performance measure set forth in this Section 3 is met.

   The Company has established as the performance measure earnings before interest, taxes, depreciation and amortization (EBITDA) generated by its continuing operations during the [year] fiscal year (beginning [date] and ending [date] (the “Measurement Period”), equal to the amount set forth in Exhibit A to this Award Agreement and as such amount may be adjusted as set forth in such Exhibit A (the “Target EBITDA”). Upon the conclusion of the Measurement Period, the Company shall calculate and determine the actual EBITDA generated by its continuing operations during the Measurement Period as set forth in Exhibit A (“Actual EDITDA”). The number of Award Shares deliverable to the Recipient will be adjusted and determined by a continuous line graph based on the following data points, which graph is included as Exhibit B:

Actual EDITDA is:	Number of Award Shares Deliverable
Less than 80% of Target EBITDA	0% of Award Shares
80% of Target EBITDA	50% of Award Shares
100% of Target EBITDA	100% of Award Shares
115% or greater of Target EBITDA	150% of Award Shares

   In the event that the Company does not generate Actual EBITDA equal to or more than 80% of Target EBITDA, then all of the RSUs shall be automatically forfeited to the Company. The Compensation Committee of the Company’s Board of Directors shall be responsible for certifying the extent to which the performance measure has been met, prior to the release of the Company’s earnings for the full [year] fiscal year.

As soon as administratively practicable after the Vesting Date, but in any event within the period ending on the later to occur of the date that is 2 1/2 months from the end of the (i) Recipient's tax year that includes the Vesting Date, or (ii) the Company's fiscal year that includes the Vesting Date, the Company shall cause its transfer agent to issue and deliver the Award Shares in the name of the Recipient, subject to payment of all applicable withholding taxes pursuant to Section 6 below.

4. **Forfeiture.**

(a) Definitions. For purposes of this Award Agreement, "Forfeiture" shall mean any forfeiture of RSUs pursuant to Section 4(b) below. For purposes of this Award Agreement, "employ" or "employment" with the Company shall include employment with a parent or subsidiary of the Company, which controls, is controlled by, or under common control of the Company.

(b) Termination of Employment.

(i) In the event that the Recipient ceases to be employed by the Company prior to the Vesting Date for any reason or no reason (except for death or disability), with or without cause, then all of the Recipient's RSUs shall be automatically and immediately forfeited and returned to the Company as of the date employment ceases.

(ii) In the event that the Recipient ceases to be employed by the Company by reason of death or disability, then the Company shall vest in the Recipient a pro rata portion of the Award Shares covered by the RSUs determined in accordance with the schedule set forth below. The balance of the Recipient's RSUs and Award Shares that are not so vested shall be automatically and immediately forfeited and returned to the Company as of the date of the Recipient's death or disability. For purposes of this Award Agreement, "disability" means that you are receiving disability benefits under the Company's Long Term Disability Coverage, as then in effect, on the date employment ceases.

Event occurs:	% of Award Shares Vested
Prior to [date]	0%
On or after [date]	33 1/3%
On or after [date]	66 2/3%
On or after [date]	100%

(c) Change in Control. In the event of a "Change in Control" that occurs (i) prior to the Vesting Date and before the last day of the Measurement Period and (ii) on a date on which the Recipient is employed by the Company, then 100% of the Recipient's RSUs that have not previously been forfeited shall become immediately vested and shall no longer be subject to the Forfeiture provisions in this Section 4, and the Company shall deliver as soon as administratively feasible but no later than 30 days after the Vesting Date that number of Award Shares to the Recipient equal to the number shown on the first page of this Award Agreement, without adjustment. In the event of a "Change in Control" that occurs (i) prior to the Vesting Date and on or after the last day of the Measurement Period and (ii) on a date on which the Recipient is employed by the Company, then 100% of the Recipient's RSUs that have not previously been forfeited shall become immediately vested and shall no longer be subject to the Forfeiture provisions in this Section 4, and the Company shall deliver as soon as administratively feasible but no later than 30 days after the Vesting Date that number of Award Shares to the Recipient equal to the number of Award Shares deliverable based on the achievement of the performance measures, as adjusted and determined in Section 3. A "Change in Control" shall have the same meaning for the purposes of this Award Agreement as set forth in Section 8 of the Plan, as the same may be amended from time to time.

5. **No Stockholder Rights.** Except as set forth in the Plan, neither the Recipient nor any person claiming under or through the Recipient shall be, or have any rights or privileges of, a stockholder of the Company in respect of the Award Shares issuable pursuant to the RSUs until the Award Shares are issued in the name of the Recipient.

6. **Withholding Taxes.** The Company's obligation to deliver Award Shares to the Recipient upon the vesting of the RSUs shall be subject to the satisfaction of all income tax (including federal, state, local and foreign taxes), social insurance, payroll tax, payment on account or other tax-related withholding requirements of any applicable jurisdiction, based on minimum statutory withholding rates for all tax purposes, including payroll and social security taxes ("Withholding Taxes"). In order to satisfy all Withholding Taxes due in connection with the award or vesting of the RSUs or the delivery of the Award Shares, the Recipient hereby irrevocably agrees to the following actions by the Company, at the Company's sole election:

(a) The Company may sell, or arrange for the sale of, such number of the Award Shares that the Recipient is entitled to receive on the Vesting Date, with no further action by the Recipient, as is sufficient to generate net proceeds at least equal to the value of the Withholding Taxes, and the Company shall retain such net proceeds in satisfaction of such Withholding Taxes. The Company shall remit to the Recipient in cash any portion of such net proceeds in excess of the value of such Withholding Taxes.

(b) The Company may retain such number of the Award Shares that the Recipient is otherwise entitled to receive on the Vesting Date, with no further action by the Recipient, by deducting and retaining from the number of Award Shares to which the Recipient is entitled that number of Award Shares as is equal to the value of the Withholding Taxes. The Recipient understands that the fair market value of the surrendered Award Shares will be determined in accordance with the Company's Stock Option and Equity Award Grant and Exercise Procedures as then in effect.

(c) The Recipient hereby appoints each of the Chief Financial Officer, General Counsel and the Secretary of the Company as his or her attorney in fact to sell or transfer the Recipient's Award Shares in accordance with this Section 6. The Recipient agrees to execute and deliver such documents, instruments and certificates as may reasonably be required in connection with the sale, transfer or retention of Award Shares pursuant to this Section 6, including an irrevocable order to sell shares authorizing a brokerage firm selected by the Company to sell the Recipient's Award Shares.

7. **No Compensation Deferral.** Neither the Plan nor this Award Agreement is intended to provide for any deferral of compensation that would be subject to Section 409A ("Section 409A") of the U.S. Internal Revenue Code of 1986, as amended. The Company reserves the right, to the extent the Company deems necessary or advisable in its sole discretion, to unilaterally amend or modify the Plan and/or this Award Agreement to ensure that all awards (including, without limitation, the RSUs) are either exempt from or complaint with the requirements of Section 409A.

8. **Administration.** The Compensation Committee of the Company's Board of Directors or other committee designated in the Plan, shall have the authority to manage and control the operation and administration of this Award Agreement. Any interpretation of the Award Agreement by any of the entities specified in the preceding sentence and any decision made by any of them with respect to the Award Agreement is final and binding.

9. **Plan Definitions.** Notwithstanding anything in this Award Agreement to the contrary, the terms of this Award Agreement shall be subject to the terms of the Plan, a copy of which has already been provided to the Recipient.

10. **Recipient's Undertakings.** In signing this Award Agreement and accepting the RSU, the Recipient acknowledges that:

(a) The Plan and this Award were established voluntarily by the Company, each is discretionary in nature, and each may be modified, amended, suspended or terminated by the Company at any time, unless otherwise provided in the Plan and this Award Agreement;

(b) The grant of RSUs is voluntary and occasional and does not create any contractual or other right to receive future awards of RSUs, or benefits in lieu of RSUs even if RSUs have been awarded repeatedly in the past or future;

(c) All decisions with respect to future grants of RSUs, if any, will be at the sole discretion of the Company;

(d) The Recipient's participation in the Plan and receipt and acceptance of the Award is voluntary;

(e) RSUs are an extraordinary item that do not constitute compensation of any kind for services of any kind rendered to the Company or to the Recipient's employer, and RSUs are outside the scope of the Recipient's employment contract, if any;

(f) RSUs are not part of normal or expected compensation or salary for any purpose, including, but not limited to, calculation of any severance, resignation, termination, redundancy, end of service payments, bonuses, long-service awards, pension or retirement benefits or similar payments and in no event should be considered as compensation for, or relating in any way to, past services for the Company or the Recipient's employer;

(g) The future value of the underlying Award Shares is unknown and cannot be predicted with certainty;

(h) The value of the Award Shares underlying the RSUs may increase or decrease in value during the period from the Award Date to the Vesting Date;

(i) In consideration of the grant of RSUs, no claim or entitlement to compensation or damages arises from termination of the RSUs or diminution in value of the RSUs or Award Shares received upon vesting of RSUs resulting from termination of the Recipient's employment by the Company or the Recipient's employer (for any reason whatsoever and whether or not in breach of local labor laws) and the Recipient irrevocably releases the Company and his or her employer from any such claim that may arise; and if, notwithstanding the foregoing, any such claim is found by a court of competent jurisdiction to have arisen, then, by signing this Award Agreement, the Recipient shall be deemed irrevocably to have waived his or her entitlement to pursue such claim; and

(j) Further, if the Recipient ceases to be an employee (whether or not in breach of local labor laws), the Recipient's right to receive RSUs and vest under the Award Agreement or Plan, if any, will terminate effective as of the date that the Recipient is no longer actively employed by the Company and will not be extended by any notice period mandated under local law (e.g., active employment would not include a period of "garden leave" or similar period pursuant to local law); and the Compensation Committee of the Company's Board of Directors shall have the exclusive discretion to determine when the Recipient is no longer actively employed for purposes of this Award Agreement and the Plan.

11. **Data Privacy Notice and Consent.** The Recipient hereby explicitly and unambiguously consents to the collection, use and transfer, in electronic or other form, of his or her personal data as described in this paragraph, by and among, as applicable, the Recipient's employer and the Company and its subsidiaries and affiliates for, among other purposes, implementing, administering and managing the Recipient's participation in the Plan. The Recipient understands that the Company and its subsidiaries hold or will hold certain personal information about the Recipient, including the Recipient's name, home address and telephone number, date of birth, social security number or identification number, salary, nationality, job title, any shares or directorships held in the Company, details of all options or awards or any other interests in shares awarded, canceled, exercised, vested, unvested or outstanding in the Recipient's name, for the purposes of managing and administering the Plan ("Data"). The Recipient further understands that the Company and its subsidiaries will

transfer Data amongst themselves as necessary for employment purposes, including implementation, administration and management of the Recipient's participation in the Plan, and that the Company and any of its subsidiaries may each further transfer Data to a broker or other stock plan service provider or other third parties assisting the Company with the processing of Data. The Recipient understands that these third parties may be located in the United States, and that the third party's country may have different data privacy laws and protections than in the Recipient's country. The Recipient authorizes them to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes described in this Section, including any requisite transfer to a broker or other stock plan service provider or other third party as may be required for the administration of the Plan and the subsequent holding of Award Shares on the Recipient's behalf. The Recipient understands that he or she may, at any time, request access to the Data, request any necessary amendments to it or refuse or withdraw the consents herein, in any case without cost, by contacting in writing the Company's Stock Option Manager at the Company's headquarters address. The Recipient understands, however, that withdrawal of consent may affect the Recipient's ability to participate in or realize the benefits of the Plan and this Award Agreement. For more information on the consequences of refusal to consent or withdrawal of consent, the Recipient understands that he or she may contact the Company's Stock Option Manager.

12. **Miscellaneous.**

(a) No Rights to Employment. The Recipient acknowledges and agrees that the vesting of the RSUs pursuant to this Award Agreement is earned only in accordance with the terms hereof. The Recipient further acknowledges and agrees that the transactions contemplated hereunder and the vesting schedule set forth herein do not constitute an express or implied promise of continued engagement as an employee for the vesting period, for any period, or at all.

(b) Unfunded Rights. The right of the Recipient to receive Award Shares pursuant to this Award Agreement is an unfunded and unsecured obligation of the Company. The Recipient shall have no rights under this Award Agreement other than those of an unsecured general creditor of the Company.

(c) Severability. The invalidity or unenforceability of any provision of this Award Agreement shall not affect the validity or enforceability of any other provision of this Award Agreement, and each other provision of this Award Agreement shall be severable and enforceable to the extent permitted by law.

(d) Waiver. Any provision for the benefit of the Company contained in this Award Agreement may be waived, either generally or in any particular instance, by the Compensation Committee of the Board of Directors of the Company.

(e) Binding Effect. This Award Agreement shall be binding upon and inure to the benefit of the Company and the Recipient and their respective heirs, executors, administrators, legal representatives, successors and assigns, subject to the restrictions on transfer set forth in this Award Agreement.

(f) Language. The English version of this Award Agreement, the Plan and any other document delivered pursuant to either the Award Agreement or the Plan, will control over any translated version of any such document in the event such translated version is different from the English version.

(g) Entire Agreement. This Award Agreement and the Plan constitute the entire agreement between the parties, and supercedes all prior agreements and understandings, relating to the subject matter of this Award Agreement.

(h) Governing Law. This Award Agreement shall be construed, interpreted and enforced in accordance with the internal laws of the State of Delaware without regard to any applicable conflicts of laws.

(i) Amendment. This Award Agreement may be amended only by written agreement between the Recipient and the Company, without the consent of any other person.

KADANT INC.
FORM OF FIRST AMENDMENT TO
DIRECTOR RESTRICTED STOCK UNITS

Preamble. This amendment is effective as of December 9, 2008 with respect to the Director Restricted Stock Unit Award Agreement granted to the Recipient named below on the date specified (the "Agreement"). This amendment is made by Kadant Inc. (the "Company") pursuant to the unilateral rights reserved under Section 7 of the Agreement to amend the Agreement to comply with Section 409A of the U.S. Internal Revenue Code.

Recipient: ___________________

RSU Award Agreement dated: ________________________

1. The last sentence of Section 3 is hereby deleted and replaced in its entirety with the following sentence (revised language appears in bold face):

"As soon as administratively practicable after the Vesting Date, but in any event within the period ending on the later to occur of the date that is **2 1/2 months** from the end of the (i) Recipient's tax year that includes the Vesting Date, or (ii) the Company's fiscal year that includes the Vesting Date, the Company shall **cause** its transfer agent to issue **and deliver** the Award Shares in the name of the Recipient, subject to payment of all applicable withholding taxes pursuant to Section 6 below."

2. Section 4(c) is hereby amended by adding the following sentence at the end of the paragraph:

"A date that a Change in Control occurs shall be a Vesting Date and the delivery requirements of Section 3 shall apply."

3. The first sentence of Section 7 shall be amended by deleting the words "an elective" immediately prior to the words "deferral of compensation" and substituting the word "any" in replacement thereof, so that the first sentence shall read in its entirety as follows:

"Neither the Plan nor this Award Agreement is intended to provide for any deferral of compensation that would be subject to Section 409A ("Section 409A") of the U.S. Internal Revenue Code of 1986, as amended."

4. The last sentence of Section 7 shall be deleted and replaced in its entirety with the following sentence (revised language appears in bold face):

"**Notwithstanding the provisions of Section 12(i),** the Company reserves the right, to the extent the Company deems necessary or advisable in its sole discretion, to unilaterally amend or modify the Plan and/or this Award Agreement to ensure that **all** awards (including, without limitation the RSUs) **are either exempt from or compliant with** the requirements of Section 409A."

IN WITNESS WHEREOF, the undersigned has signed this First Amendment effective as of the 9th day of December, 2008, by order of the Board of Directors of Kadant Inc.

KADANT INC.

By: ____________________________________
William A. Rainville
Chairman and Chief Executive Officer

Exhibit 10.19

FORM OF DIRECTOR RESTRICTED STOCK UNIT AWARD AGREEMENT

	Kadant Inc.
	ID: 52-1762325
Notice of Grant of Award	One Technology Park Drive
and Award Agreement	Westford, MA 01886

[Recipient name]	**Award Number:**	**[##]**
[Recipient address]	**Plan:**	**[##]**
	ID:	**[##]**

Effective [Date], you have been granted an award of 15,000 restricted stock units. These units are restricted until the vest date(s) shown below, at which time you will receive shares of Kadant Inc. (the Company) common stock.

The current total value of the award is $[##].

The award will vest in increments on the date(s) shown.

Shares	Full Vest
1,250	[Date – End of First Quarter]
1,250	[Date – End of Second Quarter]
1,250	[Date – End of Third Quarter]
1,250	[Date – End of Fourth Quarter]
10,000	Upon a “Change in Control” as defined herein

By your signature and the Company’s signature below, you and the Company agree that this award is granted under and governed by the terms and conditions of the Company’s Award Plan as amended and the Award Agreement, all of which are attached and made a part of this document.

Kadant Inc.	Date
[Recipient name]	Date

KADANT INC.

AWARD AGREEMENT FOR
DIRECTOR RESTRICTED STOCK UNITS
(“Award Agreement”)

1. **Preamble.** On the effective date shown on the first page of this Award Agreement (“Award Date”), the Company granted to the Recipient restricted stock units (“RSUs”) with respect to the number of shares of common stock of the Company identified on the first page of this Award Agreement (“Award Shares”), subject to the terms, conditions and restrictions set forth in this Award Agreement and the provisions of the Company’s Amended and Restated Equity Incentive Plan, as amended from time to time (“Plan”). The RSUs represent a promise by the Company to deliver the Award Shares upon vesting. Any consideration due to the Company on the issuance of Award Shares pursuant to this Award Agreement will be deemed to have been satisfied by services rendered by the Recipient to the Company during the vesting period.

2. **Restrictions on Transfer.** Unless and until the Award Shares shall have vested as provided in Section 3 below, the Recipient shall not sell, transfer, pledge, hypothecate, assign or otherwise dispose of, by operation of law or otherwise, any RSUs, or any interest therein.

3. **Vesting Date.** Subject to the terms, conditions and restrictions of this Award Agreement, including the Forfeiture provisions described in Section 4 below, the Recipient shall vest in the RSUs in accordance with the schedule set forth below (the “Vesting Date”), provided in each case that the Recipient is then, and since the Award Date has continuously been, a member of the Board of Directors of the Company. As soon as administratively practicable after the Vesting Date, but in any event within the period ending on the later to occur of the date that is 2 1/2 months from the end of the (i) Recipient’s tax year that includes the Vesting Date, or (ii) the Company’s fiscal year that includes the Vesting Date, the Company shall cause its transfer agent to issue and deliver the Award Shares in the name of the Recipient, subject to payment of all applicable withholding taxes pursuant to Section 6 below.

Vesting Schedule for Restricted Stock Units Awarded:

# of Shares	Vesting Date
1,250	[Date – End of First Quarter]
1,250	[Date – End of Second Quarter]
1,250	[Date – End of Third Quarter]
1,250	[Date – End of Fourth Quarter]
10,000	Upon a “Change-in-Control” as defined herein

In the event that the Recipient ceases to be a director of the Company prior to the Vesting Dates set forth above for the RSUs for any reason other than a “Change in Control”, then any RSUs that have not previously vested shall be immediately forfeited and returned to the Company.

Notwithstanding the foregoing, the RSUs that vest only upon a “Change in Control” as set forth in the Vesting Schedule above (the “Change in Control RSUs”) shall be deemed forfeited and returned to the Company if no “Change in Control” has occurred or no “Business Combination” (as defined in Section 8.2(c) of the Plan) has been approved by the Board of Directors of the Company during the period beginning on the first day of the Company’s second quarter of fiscal [Year] and ending on the last day of the Company’s first quarter of fiscal [Year] (the “Change in Control Period”). In the event a “Business Combination” that has been approved by the Board of Directors of the Company during the Change in Control Period is subsequently terminated or otherwise not consummated, the Change in Control RSUs shall be deemed forfeited and returned to the Company on the date of such termination or other evidence of abandonment of the Business Combination.

4. **Forfeiture.**

(a) Definitions. For purposes of this Award Agreement, “Forfeiture” shall mean any forfeiture of RSUs pursuant to Section 4(b) below.

(b) Termination of Service as a Director. In the event that the Recipient ceases to be a director of the Company prior to the Vesting Dates set forth in Section 3 above for any reason or no reason, with or without cause, then any of the Recipient’s RSUs that have not previously vested shall be automatically and immediately forfeited and returned to the Company.

(c) Change in Control. In the event of a “Change in Control” that occurs prior to the Vesting Date and on a date on which the Recipient is serving as a director of the Company, and further, with respect to the Change in Control RSUs, only as to a “Change in Control” that occurs during the Change in Control Period, then 100% of the Recipient’s RSUs that have not previously been forfeited shall become immediately vested and shall no longer be subject to the Forfeiture provisions in this Section 4. A “Change in Control” shall have the same meaning for the purposes of this Award Agreement as set forth in Section 8 of the Plan, as the same may be amended from time to time. A date that a Change in Control occurs shall be a Vesting Date and the delivery requirements of Section 3 shall apply.

5. **No Stockholder Rights.** Except as set forth in the Plan, neither the Recipient nor any person claiming under or through the Recipient shall be, or have any rights or privileges of, a stockholder of the Company in respect of the Award Shares issuable pursuant to the RSUs until the Award Shares are issued in the name of the Recipient.

6. **Withholding Taxes.** The Company’s obligation to deliver Award Shares to the Recipient upon the vesting of the RSUs shall be subject to the satisfaction of all income tax (including federal, state, local and foreign taxes), social insurance, payroll tax, payment on account or other tax-related withholding requirements of any applicable jurisdiction, based on minimum statutory withholding rates for all tax purposes, including payroll and social security taxes (“Withholding Taxes”). In order to satisfy all Withholding Taxes due in connection with the award or vesting of the RSUs or the delivery of the Award Shares, the Recipient hereby irrevocably agrees to the following actions by the Company, at the Company’s sole election:

(a) The Company may sell, or arrange for the sale of, such number of the Award Shares that the Recipient is entitled to receive on the Vesting Date, with no further action by the Recipient, as is sufficient to generate net proceeds at least equal to the value of the Withholding Taxes, and the Company shall retain such net proceeds in satisfaction of such Withholding Taxes. The Company shall remit to the Recipient in cash any portion of such net proceeds in excess of the value of such Withholding Taxes.

(b) The Company may retain such number of the Award Shares that the Recipient is otherwise entitled to receive on the Vesting Date, with no further action by the Recipient, by deducting and retaining from the number of Award Shares to which the Recipient is entitled that number of Award Shares as is equal to the value of the Withholding Taxes. The Recipient understands that the fair market value of the surrendered Award Shares will be determined in accordance with the Company's Stock Option and Equity Award Grant and Exercise Procedures as then in effect.

(c) The Recipient hereby appoints each of the Chief Financial Officer, General Counsel and the Secretary of the Company as his or her attorney in fact to sell or transfer the Recipient's Award Shares in accordance with this Section 6. The Recipient agrees to execute and deliver such documents, instruments and certificates as may reasonably be required in connection with the sale, transfer or retention of Award Shares pursuant to this Section 6, including an irrevocable order to sell shares authorizing a brokerage firm selected by the Company to sell the Recipient's Award Shares.

7. **No Compensation Deferral.** Neither the Plan nor this Award Agreement is intended to provide for any deferral of compensation that would be subject to Section 409A ("Section 409A") of the U.S. Internal Revenue Code of 1986, as amended. The Company reserves the right, to the extent the Company deems necessary or advisable in its sole discretion, to unilaterally amend or modify the Plan and/or this Award Agreement to ensure that all awards (including, without limitation, the RSUs) are either exempt from or compliant with the requirements of Section 409A.

8. **Administration.** The Compensation Committee of the Company's Board of Directors or other committee designated in the Plan, shall have the authority to manage and control the operation and administration of this Award Agreement. Any interpretation of the Award Agreement by any of the entities specified in the preceding sentence and any decision made by any of them with respect to the Award Agreement is final and binding.

9. **Plan Definitions.** Notwithstanding anything in this Award Agreement to the contrary, the terms of this Award Agreement shall be subject to the terms of the Plan, a copy of which has already been provided to the Recipient.

10. **Recipient's Undertakings.** In signing this Award Agreement and accepting the RSU, the Recipient acknowledges that:

(a) The Plan and this Award were established voluntarily by the Company, each is discretionary in nature, and each may be modified, amended, suspended or terminated by the Company at any time, unless otherwise provided in the Plan and this Award Agreement;

(b) The grant of RSUs is voluntary and occasional and does not create any contractual or other right to receive future awards of RSUs, or benefits in lieu of RSUs even if RSUs have been awarded repeatedly in the past or future;

(c) All decisions with respect to future grants of RSUs, if any, will be at the sole discretion of the Company;

(d) The Recipient's participation in the Plan and receipt and acceptance of the Award is voluntary;

(e) RSUs are an extraordinary item that do not constitute compensation of any kind for services of any kind rendered to the Company or to the Recipient's employer, and RSUs are outside the scope of the Recipient's employment contract, if any;

(f) RSUs are not part of normal or expected compensation or salary for any purpose, including, but not limited to, calculation of any severance, resignation, termination, redundancy, end of service payments, bonuses, long-service awards, pension or retirement benefits or similar payments and in no event should be considered as compensation for, or relating in any way to, past services for the Company;

(g) The future value of the underlying Award Shares is unknown and cannot be predicted with certainty;

(h) The value of the Award Shares underlying the RSUs may increase or decrease in value during the period from the Award Date to the Vesting Date;

(i) In consideration of the grant of RSUs, no claim or entitlement to compensation or damages arises from termination of the RSUs or diminution in value of the RSUs or Award Shares received upon vesting of RSUs resulting from termination of the Recipient's service as a director by the Company (for any reason whatsoever and whether or not in breach of local labor laws) and the Recipient irrevocably releases the Company from any such claim that may arise; and if, notwithstanding the foregoing, any such claim is found by a court of competent jurisdiction to have arisen, then, by signing this Award Agreement, the Recipient shall be deemed irrevocably to have waived his or her entitlement to pursue such claim; and

(j) Further, if the Recipient ceases to be a director of the Company (whether or not in breach of local labor laws), the Recipient's right to receive RSUs and vest under the Award Agreement or Plan, if any, will terminate effective as of the date that the Recipient is no longer a director of the Company and will not be extended by any notice period mandated under local law (e.g., active employment would not include a period of "garden leave" or similar period pursuant to local law); and the Compensation Committee of the Company's Board of Directors shall have the exclusive discretion to determine when the Recipient is no a director for purposes of this Award Agreement and the Plan.

11. **Data Privacy Notice and Consent.** The Recipient hereby explicitly and unambiguously consents to the collection, use and transfer, in electronic or other form, of his or her personal data as described in this paragraph, by and among, as applicable, the Company and its subsidiaries and affiliates for, among other purposes, implementing, administering and managing the Recipient's participation in the Plan. The Recipient understands that the Company and its subsidiaries hold or will hold certain personal information about the Recipient, including the Recipient's name, home address and telephone number, date of birth, social security number or identification number, salary, nationality, job title, any shares or directorships held in the Company, details of all options or awards or any other interests in shares awarded, canceled, exercised, vested, unvested or outstanding in the Recipient's name, for the purposes of managing and administering the Plan ("Data"). The Recipient further understands that the Company and its subsidiaries will transfer Data amongst themselves as necessary for employment purposes, including implementation, administration and management of the Recipient's participation in the Plan, and that the Company and any of its subsidiaries may each further transfer Data to a broker or other stock plan service provider or other third parties assisting the Company with the processing of Data. The Recipient understands that these third parties may be located in the United States, and that the third party's country may have different data privacy laws and protections than in the Recipient's country. The Recipient authorizes them to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes described in this Section, including any requisite transfer to a broker or other stock plan service provider or other third party as may be required for the administration of the Plan and the subsequent holding of Award Shares on the Recipient's behalf. The Recipient understands that he or she may, at any time, request access to the Data, request any necessary amendments to it or refuse or withdraw the consents herein, in any case without cost, by contacting in writing the Company's Stock Option Manager at the Company's headquarters address. The Recipient understands, however, that withdrawal of consent may affect the Recipient's ability to participate in or realize the benefits of the Plan and this Award Agreement. For more information on the consequences of refusal to consent or withdrawal of consent, the Recipient understands that he or she may contact the Company's Stock Option Manager.

12. **Miscellaneous.**

(a) No Rights to Employment. The Recipient acknowledges and agrees that the vesting of the RSUs pursuant to this Award Agreement is earned only in accordance with the terms hereof. The Recipient further acknowledges and agrees that the transactions contemplated hereunder and the vesting schedule set forth herein do not constitute an express or implied promise of continued engagement as a director for the vesting period, for any period, or at all.

(b) Unfunded Rights. The right of the Recipient to receive Award Shares pursuant to this Award Agreement is an unfunded and unsecured obligation of the Company. The Recipient shall have no rights under this Award Agreement other than those of an unsecured general creditor of the Company.

(c) Severability. The invalidity or unenforceability of any provision of this Award Agreement shall not affect the validity or enforceability of any other provision of this Award Agreement, and each other provision of this Award Agreement shall be severable and enforceable to the extent permitted by law.

(d) Waiver. Any provision for the benefit of the Company contained in this Award Agreement may be waived, either generally or in any particular instance, by the Compensation Committee of the Board of Directors of the Company.

(e) Binding Effect. This Award Agreement shall be binding upon and inure to the benefit of the Company and the Recipient and their respective heirs, executors, administrators, legal representatives, successors and assigns, subject to the restrictions on transfer set forth in this Award Agreement.

(f) Language. The English version of this Award Agreement, the Plan and any other document delivered pursuant to either the Award Agreement or the Plan, will control over any translated version of any such document in the event such translated version is different from the English version.

(g) Entire Agreement. This Award Agreement and the Plan constitute the entire agreement between the parties, and supercedes all prior agreements and understandings, relating to the subject matter of this Award Agreement.

(h) Governing Law. This Award Agreement shall be construed, interpreted and enforced in accordance with the internal laws of the State of Delaware without regard to any applicable conflicts of laws.

(i) Amendment. This Award Agreement may be amended only by written agreement between the Recipient and the Company, without the consent of any other person.

Exhibit 21

Kadant Inc.
Subsidiaries of the Registrant

At March 1, 2009, the Registrant owned the following companies:

Name	State or Jurisdiction of Incorporation	Percent of Ownership
ArcLine Products LLC.	New York	100
Kadant Black Clawson Inc.	Delaware	100
Kadant Fibergen Inc.	Delaware	100
Fibergen Securities Corporation	Massachusetts	100
Kadant GranTek Inc.	Delaware	100
Kadant Composites LLC	Delaware	100
Kadant International Holdings Inc.	Delaware	100
Kadant Asia Holdings Inc.	Mauritius	100
Kadant Light Machinery (Jining) Co. Ltd.	China	100
Kadant Pulp & Paper Equipment (Yanzhou) Co. Ltd.	China	100
Kadant (Gibraltar) Limited	Gibraltar	100
Kadant International LLC Luxembourg SCS (62.2% owned directly by Kadant (Gibraltar) Limited; 37.7% owned by Kadant Johnson Inc.; and less than 1% owned directly by each of Kadant International Holdings Inc. and Kadant International LLC)	Luxembourg	100
Kadant Luxembourg SarL	Luxembourg	100
Kadant (Cyprus) Limited	Cyprus	100
Kadant Johnson Europe B.V.	Netherlands	100
Kadant Canada Corp.	Nova Scotia, Canada	100
Kadant Cyprus (Canada) Limited	Cyprus	100
Kadant U.K. Holdings Limited	England	100
Fibertek U.K. Limited	England	100
Kadant U.K. Limited	England	100
D.S.T. Pattern Engineering Company Limited	England	100
Vickerys Limited	England	100
Winterburn Limited	England	100
Kadant Mexico LLC	Delaware	100
Kadant Mexico, S.A. de C.V.	Mexico	100
Kadant Johnson Deutschland GmbH	Germany	100
Kadant Johnson France B.V.	Netherlands	100
Kadant Johnson Scandinavia AB	Sweden	100
Kadant Johnson Schweiz AG	Switzerland	100
Kadant Johnson Systems International Ltd.	England	100
Kadant Johnson Systems International S.r.l.	Italy	100
Johnson Corporation (JoCo) Limited	England	100
Johnson-Fluiten S.r.l.	Italy	50
Kadant Lamort	France	100
Kadant BC Lamort UK	England	100
Kadant Cyclotech AB	Sweden	100
Kadant Lamort AB	Sweden	100

Name	State or Jurisdiction of Incorporation	Percent of Ownership
Kadant Lamort GmbH	Germany	100
Kadant Lamort S.A.	Spain	100
Kadant Lamort S.r.l.	Italy	100
Kadant International LLC	Delaware	100
Kadant Johnson Inc.	Michigan	100
Kadant Fiberline Commercial (Beijing) Co., Ltd.	China	100
Kadant Johnson Argentina S.r.l.	Argentina	100
Kadant Johnson China-TZ Holding Inc.	Michigan	100
Tengzhou Feixuan Rotary Joint Manufacturing Co., Ltd.	China	100
Kadant Johnson China-WX Holding Inc.	Michigan	100
Kadant Johnson (Wuxi) Technology Ltd.	China	100
Kadant Johnson Latin America Holding Inc.	Michigan	100
Kadant Johnson Latin America S.A.	Brazil	100
Kadant Johnson Southeast Asia Pty. Limited	Australia	90
Kadant Johnson Australia Pty. Limited	Australia	100
Kadant Johnson Corporation Asia Pacific Pty. Ltd.	Australia	100
Kadant Johnson Holding Inc.	Michigan	100
The Johnson Corporation Mexico S.A. de C.V.	Mexico	100
Kadant Web Systems Inc.	Massachusetts	100
Fiberprep Inc. (31.05% of which shares are owned directly by Kadant Lamort)	Delaware	100
Fiberprep Securities Corporation	Massachusetts	100

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statements (Forms S-8 Nos. 33-67190, 33-67192, 33-67194, 33-83718, 333-80509, 333-48498, 333-65206, 333-102223, 333-102224, 333-142247, and 333-142247) of Kadant Inc. of our reports dated March 3, 2009, with respect to the consolidated financial statements and schedule of Kadant Inc., and the effectiveness of internal control over financial reporting of Kadant Inc., included in the Annual Report (Form 10-K) for the year ended January 3, 2009.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 3, 2009

CERTIFICATION

I, William A. Rainville, certify that:

1. I have reviewed this Annual Report on Form 10-K for the year ended January 3, 2009 of Kadant Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 9, 2009

/s/ WILLIAM A. RAINVILLE

William A. Rainville
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Thomas M. O'Brien, certify that:

1. I have reviewed this Annual Report on Form 10-K for the year ended January 3, 2009 of Kadant Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 9, 2009

/s/ THOMAS M. O'BRIEN

Thomas M. O'Brien
Chief Financial Officer

Exhibit 32

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to 18 U.S.C. Section 1350, the undersigned, William A. Rainville, Chief Executive Officer, and Thomas M. O'Brien, Chief Financial Officer, of Kadant Inc., a Delaware corporation (the "Company"), do hereby certify, to our best knowledge and belief, that:

The Annual Report on Form 10-K for the year ended January 3, 2009 of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in this Annual Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: March 9, 2009

/s/ WILLIAM A. RAINVILLE

William A. Rainville
Chief Executive Officer

/s/ THOMAS M. O'BRIEN

Thomas M. O'Brien
Chief Financial Officer

This certification accompanies this Annual Report on Form 10-K pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by such Act, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the Company specifically incorporates it by reference.