UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

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

For the fiscal year ended September 30, 2006

OR

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

For the transition period from __________ to __________

Commission file number: 1-10596

ESCO Technologies Inc.

(Exact name of registrant as specified in its charter)

Missouri **(State or other jurisdiction of incorporation or organization)**	43-1554045 **(I.R.S. Employer Identification No.)**
9900A Clayton Road St. Louis, Missouri **(Address of principal executive offices)**	63124-1186 **(Zip Code)**

Registrant's telephone number, including area code:

(314) 213-7200

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.01 per share	New York Stock Exchange, Inc.
Preferred Stock Purchase Rights	New York Stock Exchange, Inc.

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 o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. o

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 o

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 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer o Non-accelerated filer o

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

Aggregate market value of the Common Stock held by non-affiliates of the registrant as of the close of business on March 31, 2006: $1,277,229,653*.

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* For purpose of this calculation only, without determining whether the following are affiliates of the registrant, the registrant has assumed that (i) its directors and executive officers are affiliates, and (ii) no party who has filed a Schedule 13D or 13G is an affiliate.

Number of shares of Common Stock outstanding at December 11, 2006: 25,889,335.

DOCUMENTS INCORPORATED BY REFERENCE:

1. Portions of the registrant's Annual Report to Stockholders for fiscal year ended September 30, 2006 (the "2006 Annual Report") (Parts I and II).
2. Portions of the registrant's Proxy Statement dated December 20, 2006 (the "2007 Proxy Statement") (Part III).

ESCO TECHNOLOGIES INC.
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PART I

Item 1. Business

THE COMPANY

ESCO Technologies Inc. (“ESCO”) is a producer of engineered products and systems sold to customers worldwide, primarily for industrial and commercial applications. ESCO operates in three operating segments which, together with the operating subsidiaries within each segment, are as follows:

Filtration/Fluid Flow:
Filtertek Inc. (including its Tek Packaging Division)
Filtertek BV
Filtertek do Brasil Industria E Commercio Ltda.
Filtertek SA
PTI Technologies Inc. (“PTI”)
VACCO Industries (“VACCO”)
ESCO Electronica De Mexico, S.A. de C.V. (“ESCOMEX”)

Communications:
Distribution Control Systems, Inc. (“DCSI”)
Distribution Control Systems Caribe, Inc.
Hexagram, Inc. (“Hexagram”)
Nexus Energy Software, Inc. (“Nexus”)
Comtrak Technologies, L.L.C. (“Comtrak”)

Test:
ETS-Lindgren L.P. (“ETS”)
Lindgren RF Enclosures, Inc. (“Lindgren”)
Euroshield OY
Ray Proof Limited
Beijing Lindgren ElectronMagnetic Technology Co., Ltd. (“Beijing Lindgren”)
ETS-Lindgren Japan, Inc.

All of the Filtertek entities listed above and ESCOMEX are hereinafter collectively referred to as “Filtertek”. All of the Test segment entities listed above are hereinafter collectively referred to as “ETS-Lindgren”.

The above operating subsidiaries are engaged primarily in the research, development, manufacture, sale and support of the products and systems described below, and are subsidiaries of ESCO Technologies Holding Inc., a wholly-owned direct subsidiary of ESCO. ESCO and its direct and indirect subsidiaries are hereinafter referred to collectively as the “Company”. The Company’s businesses are subject to a number of risks and uncertainties, including without limitation those discussed in Item 1A below. See also “Management’s Discussion and Analysis” appearing in the 2006 Annual Report, which is herein incorporated by reference, and “Forward-Looking Information” below.

Effective November 29, 2005, ESCO acquired Nexus for a purchase price of approximately $29 million plus contingent consideration based on future sales. Nexus, with headquarters in Wellesley, Massachusetts, is primarily a producer of software for energy meter applications.

Effective February 1, 2006, ESCO acquired Hexagram for a purchase price of approximately $66 million plus contingent consideration based on future sales. Hexagram, located in Cleveland, Ohio, is a producer of radio frequency (“RF”) fixed network automatic meter reading (“AMR”) systems.

DISCONTINUED OPERATIONS

The Company's former microfiltration and separations businesses ("MicroSep Business") consisted of PTI Advanced Filtration Inc. (Oxnard, California), PTI Technologies Limited (Sheffield, England) and PTI S.p.A. (Milan, Italy). The MicroSep Business produced membrane-based microfiltration and separation products and systems for use in process filtration and separation applications. In fiscal 2004, the MicroSep Business accounted for approximately $29 million in net sales.

Effective April 2, 2004, the Company completed the sale of PTI Advanced Filtration Inc. and PTI Technologies Limited to domnick hunter group plc for $18 million in cash. On June 8, 2004, the Company completed the sale of PTI S.p.A. to a group of investors comprised of that subsidiary's senior management for $5.3 million. The MicroSep Business is accounted for as a discontinued operation in the Consolidated Financial Statements in the 2004 period in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets".

The following sections of this Item 1 refer to the Company's continuing operations, except where noted. Accordingly, dollar amounts and percentages presented below in this Item 1 for all periods reflect continuing operations by excluding the MicroSep Business. See Note 3 of the Notes to Consolidated Financial Statements in the 2006 Annual Report, which Note is herein incorporated by reference.

PRODUCTS

The Company's products are described below. See Note 15 of the Notes to Consolidated Financial Statements in the 2006 Annual Report for financial information regarding segments, which Note is herein incorporated by reference.

FILTRATION/FLUID FLOW

The Filtration/Fluid Flow segment accounted for approximately 38%, 40% and 41% of the Company's total revenue in fiscal years 2006, 2005 and 2004, respectively.

Filtertek develops and manufactures a broad range of specialized filtration and fluid/flow products at its facilities in North America, South America and Europe. Filtertek's products, which are centered around its insert injection-molding technology wherein a filter medium is inserted into the tooling prior to injection-molding of the filter housing, have widespread applications in the medical and healthcare, automotive fluid system, consumer appliance and other commercial and industrial markets. Typical Filtertek customers may require daily production of thousands of units, at very high levels of quality, that are generally produced in highly-automated manufacturing cells. Many of Filtertek's products are produced utilizing patented designs or proprietary product or process design, or both. Filtertek's products are typically supplied to original equipment manufacturers under long-term contracts. The Tek Packaging Division of Filtertek Inc. produces highly engineered thermal-formed and security packaging products for medical, food and electronics products.

PTI is a leading supplier of filtration products serving the commercial aerospace, military aerospace and various industrial markets. The industrial markets include chemical processing, automotive and mobile equipment. Products include filter elements, assemblies, modules, indicators and other related components. All products must meet stringent quality requirements and withstand severe operating conditions. Product applications include aircraft and mobile equipment hydraulic systems, aircraft engines, plant equipment and automotive transmissions. PTI supplies product worldwide to original equipment manufacturers and the U.S. government under long term contracts, and to the commercial aftermarkets through distribution channels.

VACCO supplies flow control products to the aerospace industry for use in aircraft, satellite propulsion systems, satellite launch vehicles and the space shuttle. VACCO also uses its etched disc technology to produce quiet valves and manifolds for U.S. Navy applications.

COMMUNICATIONS

The Communications segment accounted for approximately 34%, 32% and 33% of the Company's total revenue in fiscal years 2006, 2005 and 2004, respectively.

DCSI is a leading manufacturer of two-way power line communication systems for the electric utility industry (the "TWACS® systems"), which are composed of equipment (primarily meter modules and equipment for central stations and substations), software and support services. The TWACS Next Generation ("TNG") software is being developed jointly with a third-party contractor. This development continued in fiscal 2006, leading to the commercial release of its second version, which was delivered to a second customer location and underwent operational testing. Currently, additional versions of the TNG software are under development and are scheduled for commercial release in fiscal 2007. The TWACS systems provide electric utilities with a patented communication technology for automatic meter reading, load control, interval data, outage assessment/restoration monitoring, remote service disconnect/connect, time-of-use data for critical peak pricing, tamper/theft detection and pre-paid metering. Revenue from the TWACS systems, which may be considered a class of similar products, accounted for approximately 26%, 28% and 31% of the Company's total revenue in fiscal years 2006, 2005 and 2004, respectively. In November 2005, DCSI received a contract from Pacific Gas and Electric Company ("PG&E") in support of the electric portion of PG&E's Advanced Metering Infrastructure ("AMI") Project. The current AMI program plan provides for the coverage of up to approximately five million electric endpoints over the five-year full deployment period. System testing of a small test system was successfully completed in fiscal year 2006, and PG&E received approval from the California Public Utility Commission for the entire AMI project. DCSI has agreed to deliver to PG&E versions of its newly developed TNG software as they become available and are tested. Delivery of the final version, for which DCSI has committed, is currently anticipated in the fourth quarter of fiscal 2007. The contract provides for remedies including, but not limited to, liquidated damages in the event of DCSI's delayed development or delivery of hardware and software. The total anticipated contract value from commencement through the five-year full deployment period is approximately $310 million. Equipment will be purchased by PG&E only upon issuance of purchase orders. See Item 1.A Risk Factors.

Hexagram provides, through its STAR® network, wireless RF data communications systems primarily to gas and water utilities for automatic meter reading applications. In November 2005, Hexagram received a contract from PG&E to provide its communications system for the gas meter portion of PG&E's AMI Project. The total anticipated contract revenue through the full five-year deployment is approximately $225 million. This contract is subject to contingencies and uncertainties similar to those associated with the DCSI — PG&E contract described above except that the TNG software is not applicable to this contract.

Nexus provides energy companies with software solutions that add value to their existing billing and metering infrastructure to allow both the energy company and its customers to better manage energy-driven transactions and decision-making. Nexus' analytics-based software applications are used by over 85 major energy organizations worldwide. In fiscal 2006, Nexus implemented a Meter Data Management System for PPL Electric Utilities that integrates with the TWACS® system, and processes and manages hourly data collected from 1.375 million meters.

Comtrak manufactures advanced video security monitoring systems for commercial and industrial applications. Comtrak is continuing to work jointly with ADT Security Services, Inc., who is selling this system under its SecurVision® trademark to a variety of markets.

TEST

The Test segment accounted for approximately 28%, 28% and 26% of the Company's total revenue in fiscal years 2006, 2005 and 2004, respectively.

ETS-Lindgren designs and manufactures products to measure and contain magnetic, electromagnetic and acoustic energy. It supplies customers with a broad range of isolated environments including RF test enclosures, acoustic test enclosures, RF and magnetically shielded rooms, secure communication facilities and broadcast and recording studios. Many of these facilities include proprietary features such as shielded doors and windows. ETS-Lindgren also provides the design, program management, installation and integration services required to successfully complete these types of facilities.

ETS-Lindgren also supplies customers with a broad range of components including RF absorptive materials, RF filters, active compensation systems, antennas, antenna masts, turntables and electric and magnetic probes, RF test cells, proprietary measurement software and other test accessories required to perform a variety of tests. ETS-Lindgren also offers a variety of services including calibration for antennas and field probes, chamber certification, field surveys, customer training and a variety of product tests. ETS-Lindgren operates the following accredited test labs: American Association for Laboratory Accreditation (“A2LA”), National Voluntary Laboratory Accreditation Program (“NAVLAP”) and CTIA-The Wireless Association (“CTIA”). In addition, ETS-Lindgren serves the acoustics, medical, health and safety, electronics, wireless communications, automotive and defense markets.

MARKETING AND SALES

The Filtration/Fluid Flow and Test segments’ products generally are distributed to customers through a domestic and foreign network of distributors, sales representatives and in-house salespersons. DCSI’s sales to investor-owned utilities are primarily made directly to the utilities. DCSI primarily utilizes distributors and sales representatives to sell its systems to the electric utility cooperative and municipal markets. Hexagram has an exclusive agreement with Neptune Technology Group, Inc. for the distribution of its products to its water utility customers, and utilizes in-house salespersons to cover electric, gas and combination utilities. Nexus markets its products utilizing its in-house sales force.

The Company’s international sales accounted for approximately 22%, 24% and 22% of the Company’s total sales in the fiscal years ended September 30, 2006, 2005 and 2004, respectively. See Note 15 of the Notes to Consolidated Financial Statements in the 2006 Annual Report for financial information regarding geographic areas, which Note is herein incorporated by reference.

Some of the Company’s products are sold directly or indirectly to the U.S. Government under contracts with the Army, Navy and Air Force and subcontracts with prime contractors of such entities. Direct and indirect sales to the U.S. Government accounted for approximately 6%, 8% and 8% of the Company’s total sales in the fiscal years ended September 30, 2006, 2005 and 2004, respectively.

INTELLECTUAL PROPERTY

The Company owns or has other rights in various forms of intellectual property (i.e., patents, trademarks, service marks, copyrights, mask works, trade secrets and other items). As a major supplier of engineered products to growing industrial and commercial markets, the Company emphasizes developing intellectual property and protecting its rights therein. However, the scope of protection afforded by intellectual property rights, including those of the Company, is often uncertain and involves complex legal and factual issues. Some intellectual property rights, such as patents, have only a limited term. Also, there can be no assurance that third parties will not infringe or design around the Company’s intellectual property. Policing unauthorized use of intellectual property is difficult, and copyright infringement is a persistent problem for many companies, particularly in some international markets. In addition, the Company may not elect to pursue an unauthorized user due to the high costs and uncertainties associated with litigation. Further, there can be no assurance that courts will ultimately hold issued patents valid and enforceable. See Item 1.A Risk Factors.

With respect to the Filtration/Fluid Flow segment, an increasing number of products are based on patented or otherwise proprietary technology that sets them apart from the competition. Of particular importance to Filtertek is a U.S. patent covering certain transmission sump filters, which will expire in 2009. Also, Filtertek receives significant income from licensing and cost recovery efforts concerning its U.S. patent on certain needle-free medical connection devices, having claims which will expire on various dates between 2011 and 2013. VACCO’s proprietary quieting technology, which it protects as trade secrets, is a significant differentiator for products supplied to the U.S. Navy submarine fleet. In June 2005, the Company abandoned its plans to commercialize certain PTI sensor products, resulting in the abandonment of certain related patents and a related license agreement. See “Management’s Discussion and Analysis”—“Asset Impairment-2005” appearing in the 2006 Annual Report.

In the Communications segment, many of the products are based on patented or otherwise proprietary technology, including the Company's TWACS technology. The TWACS systems are protected primarily by a number of patents expiring on various dates ending in 2017. Patents covering significant aspects of the TWACS technology will expire in 2007 and 2010 for outbound signal reception, 2007 for inbound signal detection, and 2017 for inbound signal generation. The Communications segment policy is to seek patent and/or other forms of intellectual property protection on new and improved products, components of products and methods of operation for its businesses, as such developments are made. The Company plans to protect the TNG software as trade secrets. Hexagram holds two significant patents which cover the operation of its STAR® network communications systems. These will expire in 2015 and 2016.

In the Test segment, patent protection has been sought for significant inventions. Examples of such inventions include novel designs for window and door assemblies used in shielded enclosures and anechoic chambers as well as improved acoustic techniques for sound isolation.

The Company considers its patent and other intellectual property to be of significant value in each of its segments. The Communications segment owns intellectual property, including its TWACS technology, which it deems necessary or desirable for the manufacture, use or sale of its products. See the references to the TNG software above in this section and in "Communications" on page 3 of this report. No other segment is materially dependent on any single patent, group of patents or other intellectual property.

BACKLOG

Total Company backlog at September 30, 2006 was $253.4 million, representing an increase of $20.3 million (8.7%) from the beginning of the fiscal year backlog of $233.1 million. The backlog of firm orders at September 30, 2006 and September 30, 2005, respectively, was: $78.6 million and $80.5 million for Filtration/Fluid Flow; $119.0 million and $87.8 million for Communications; and $55.8 million and $64.8 million for Test. As of September 30, 2006, it is estimated that domestic customers accounted for approximately 81% of the Company's total firm orders, and international customers accounted for approximately 19%. Of the Company's total backlog of orders at September 30, 2006, approximately 77% is expected to be completed in the fiscal year ending September 30, 2007.

PURCHASED COMPONENTS AND RAW MATERIALS

The Company's products require a wide variety of components and materials. Although the Company has multiple sources of supply for most of its materials requirements, certain components and raw materials are supplied by sole-source vendors, and the Company's ability to perform certain contracts depends on their performance. In the past, these required raw materials and various purchased components generally have been available in sufficient quantities. However, in each of the Company's segments, there are instances of some risk of shortages of materials or components due to reliance on sole or limited source of supply. See Item 1.A Risk Factors.

The Filtration/Fluid Flow segment purchases supplies from a wide array of vendors. In most instances, multiple vendors of raw materials are screened during a qualification process to ensure that there will not be an interruption of supply should one of them discontinue operations. Nonetheless, in some situations, there is a risk of shortages due to reliance on a limited number of suppliers or because of price fluctuations due to the nature of the raw materials, as in the case of petroleum-based resins utilized by Filtertek.

In the Communications segment, DCSI has arrangements with three independent manufacturers which produce and supply substantially all of DCSI's end-products. Two of these manufacturers are industry leaders with world-wide operations. Each of these manufacturers is directed by DCSI to purchase certain unique raw material components from suppliers designated by DCSI. DCSI also has contracts with certain of the raw material suppliers, directing them to supply such raw materials to DCSI's manufacturers. Hexagram has a contract with an independent manufacturer which produces and supplies substantially all of Hexagram's end-products, as well as contracts with several of the suppliers of the raw materials that are incorporated into such end-products. Hexagram is in the process of finalizing a new contract with one of the primary suppliers used by DCSI, which will be a second source for the production of Hexagram's end-products. The Company believes that the above-described manufacturers and suppliers will be reliable sources for DCSI's and Hexagram's end-products for the foreseeable future.

The Test segment is a vertically integrated supplier of EM shielding products, producing most of its critical RF components. However, this segment purchases significant quantities of raw materials such as steel, copper, nickel and wood. Accordingly, the segment is subject to price fluctuations in the worldwide raw materials markets. In fiscal 2006, this segment experienced significant price increases in the metal markets as compared to the prior year.

COMPETITION

Competition in the Company's major markets is broadly based and global in scope. The Company faces intense competition from a large number of companies for nearly all of its products. Competition can be particularly intense during periods of economic slowdown, and this has been experienced in the past in some of the Filtration/Fluid Flow markets. Although the Company is a leading supplier in several of the markets it serves, it maintains a relatively small share of the business in many of the other markets it serves. Individual competitors range in size from annual revenues of less than $1 million to billion dollar enterprises. Because of the specialized nature of the Company's products, its competitive position with respect to its products cannot be precisely stated. However, DCSI is believed to be a leading supplier in the fixed network segment of the automatic meter reading ("AMR") market. This fixed network segment comprises a substantial part of the electric portion of the total AMR market for electric utilities. Substantial efforts are required in order to maintain existing business levels. In the Company's major served markets, competition is driven primarily by quality, technology, price and delivery performance. See Item 1.A Risk Factors.

Pall Corporation, SPX Filtran and SoFrance are the primary competitors in the Filtration/Fluid Flow markets. Other significant competitors in these markets include Clarcor Inc., Cummins Filtration and Moog Inc.

Primary competitors of the Communications segment in the utility communications market include Itron, Inc., Hunt Technologies Inc., Cellnet Technology Inc., Cannon Technologies Inc., Sensus Metering Systems Inc., Elster Electricity, L.L.C, Comverge, Inc. and Lodestar Corporation.

The Test segment is the global leader in the EM shielding market. Significant competitors in this served market include TDK RF Solutions Inc., Albatross GmbH, IMEDCO AG and Cuming Corporation.

RESEARCH AND DEVELOPMENT

Research and development and the Company's technological expertise are important factors in the Company's business. Research and development programs are designed to develop technology for new products or to extend or upgrade the capability of existing products, and to enhance their commercial potential.

The Company performs research and development at its own expense, and also engages in research and development funded by customers. For the fiscal years ended September 30, 2006, 2005 and 2004, total Company-sponsored research and development expenses were approximately $20.0 million, $16.8 million and $12.2 million, respectively. Total customer-sponsored research and development expenses were approximately $6.3 million, $5.7 million and $6.1 million for the fiscal years ended September 30, 2006, 2005 and 2004, respectively. All of the foregoing expense amounts exclude certain engineering costs primarily associated with product line extensions, modifications and maintenance, which amounted to approximately $9.1 million, $7.8 million and $9.6 million for the fiscal years ended September 30, 2006, 2005 and 2004, respectively.

ENVIRONMENTAL MATTERS

The Company is involved in various stages of investigation and cleanup relating to environmental matters. It is very difficult to estimate the potential costs of such matters and the possible impact of these costs on the Company at this time due in part to: the uncertainty regarding the extent of pollution; the complexity of Government laws and regulations and their interpretations; the varying costs and effectiveness of alternative cleanup technologies and methods; the uncertain level of insurance or other types of cost recovery; and in the case of off-site waste disposal facilities, the uncertain level of the Company's relative involvement and the possibility of joint and several liability with other contributors under applicable law. Based on information currently available, the Company does not believe that the aggregate costs involved in the resolution of any of its environmental matters will have a material adverse effect on the Company's financial statements.

GOVERNMENT CONTRACTS

The Company's contracts with the U.S. Government and subcontracts with prime contractors of the U.S. Government are primarily firm fixed-price contracts under which work is performed and paid for at a fixed amount without adjustment for the actual costs experienced in connection with the contracts. Therefore, unless the customer actually or constructively alters or impedes the work performed, all risk of loss due to cost overruns is borne by the Company. All Government prime contracts and virtually all of the Company's subcontracts provide that they may be terminated at the convenience of the Government. Upon such termination, the Company is normally entitled to receive equitable compensation. See "Marketing And Sales" in this Item 1 and Item 1.A Risk Factors for additional information regarding Government contracts.

EMPLOYEES

As of November 30, 2006, the Company employed approximately 2,685 persons.

FINANCING

On October 6, 2004, the Company entered into a $100 million five-year revolving credit facility with a $50 million increase option. This facility is available for direct borrowings and/or the issuance of letters of credit, and is provided by a group of six banks, led by Wells Fargo Bank as agent, with a maturity of October 6, 2009. The facility is secured by the unlimited guaranty of the Company's material domestic subsidiaries and a 65% pledge of the material foreign subsidiaries' share equity. See "Management's Discussion and Analysis — Capital Resources and Liquidity" in the 2006 Annual Report, and Note 10 of the Notes to Consolidated Financial Statements in the 2006 Annual Report, which information is herein incorporated by reference.

HISTORY OF THE BUSINESS

ESCO was incorporated in Missouri in August 1990 as a wholly-owned subsidiary of Emerson Electric Co. ("Emerson") to be the indirect holding company for several Emerson subsidiaries, which were primarily in the defense business. Ownership of ESCO and its subsidiaries was distributed on October 19, 1990 by Emerson to its shareholders through a special distribution. Since that time, through a series of acquisitions and divestitures, the Company has shifted its primary focus from defense contracting to the supply of engineered products marketed to industrial and commercial users. Effective July 10, 2000, ESCO changed its name from ESCO Electronics Corporation to ESCO Technologies Inc.

The MicroSep Business, which was divested in fiscal 2004, is discussed under "Discontinued Operations" in this Item 1.

AVAILABLE INFORMATION

The Company makes available free of charge through its Internet website, www.escotechnologies.com, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission.

Item 1A. Risk Factors

This Form 10-K, including Item 1 “Business,” Item 2 “Properties”, Item 3 “Legal Proceedings” and Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (incorporated by reference to “Management’s Discussion and Analysis” appearing in the 2006 Annual Report), contains “forward-looking statements” within the meaning of the safe harbor provisions of the federal securities laws. In addition to the risks and uncertainties discussed elsewhere in this Form 10-K, the following are important risk factors which could cause actual results and events to differ materially from those contained in any forward-looking statements.

A SIGNIFICANT PORTION OF COMMUNICATIONS SEGMENT REVENUES IS GENERATED BY A LIMITED NUMBER OF LARGE CONTRACTS.

A significant portion of the Communications segment’s business is dependent on several large contracts with customers. The largest of these are two contracts to sell electric and gas automatic meter reading systems to PG&E over a period of approximately five years. These projects, which represent a potential high source of revenue, are subject to cancellation or reduction in volume by PG&E, delays, regulatory actions and the Company’s ability to develop advanced products and successfully perform the contracts. The loss of revenue which would result from cancellations, delays, reductions, regulatory actions or the Company’s failure to perform in connection with these projects could have a material adverse effect on the Company’s business, results of operations and financial condition as a whole.

FAILURE OR DELAY IN NEW PRODUCT DEVELOPMENT COULD REDUCE THE COMPANY’S FUTURE SALES.

Much of the Company’s business is dependent on the continuous development of new products and technologies to meet the changing needs of the Company’s markets on a cost-effective basis. Many of these markets are highly technical from an engineering standpoint, and the relevant technologies are subject to rapid change. For example, the continued development of the TWACS Next Generation (“TNG”) software is critical to the continued sales growth of DCSI. Failure to deliver the final version of TNG, to which DCSI has committed under the PG&E contract, could constitute an event of default and adversely impact expected revenues.

If the Company fails to timely enhance existing products or develop new products, sales opportunities could be lost, which would adversely affect business. In addition, in some existing contracts with customers, the Company has made commitments to develop and deliver new products. If the Company fails to meet these commitments, the default could result in the imposition of contractual penalties including termination. The inability to enhance existing products in a timely manner could make the products less competitive, while the inability to successfully develop new products may limit growth opportunities. Delays in product development may also require greater investment in research and development. Increased costs associated with new product development and product enhancements could adversely affect operating results. The costs of new product development may not be recoverable if demand for the products is not as anticipated.

CERTAIN MANUFACTURING OPERATIONS ARE DEPENDENT ON A SMALL NUMBER OF THIRD-PARTY SUPPLIERS

A significant part of the Communications segment’s manufacturing operations relies on a small number of third-party manufacturers to supply the segment’s products. For example, DCSI has arrangements with three manufacturers which produce and supply substantially all of DCSI’s end-products. Two of these suppliers are located in Mexico. A significant disruption (for example, a strike) in the supply of those products could negatively affect the timely delivery of DCSI's products to customers and future sales. Comtrak currently relies on a single source for a major portion of its products.

Certain of the Company's other businesses are dependent upon sole source or a limited number of third-party manufacturers of parts and components. Many of these suppliers are small businesses. Since alternative supply sources are limited, this increases the risk of adverse impacts on the Company's production schedules and profits if the Company's suppliers default in fulfilling their price, quality or delivery obligations.

MOST COMMUNICATIONS SEGMENT SALES ARE TO OR FOR THE UTILITY INDUSTRY, KNOWN FOR LONG SALES CYCLES AND UNCERTAINTY, WHICH COULD AFFECT THE TIMING OF REVENUE

Most of the Communications segment's sales are to or for the utility industry, where sales cycles are long and unpredictable. Most sales involve large dollar amounts, and are marked by extended and complex competitive procurements. These factors often cause delays in the timing of sales, and such delays could result in order postponement, reduction in size or cancellation, thereby reducing the Company's future revenue.

PRODUCT DEFECTS COULD RESULT IN COSTLY FIXES, LITIGATION AND DAMAGES

If there are claims related to defective products (under warranty or otherwise), particularly in a product recall situation, the Company could be faced with significant expenses in replacing or repairing the product. For example, the DCSI and Hexagram meter modules are installed in thousands of residences and other buildings. The replacement/repair costs for such problems could have a material adverse effect on the Company's financial condition. In addition, if a dispute over product claims cannot be settled, arbitration or litigation may result, involving attorneys' fees and the potential of damage awards.

INCREASES IN RAW MATERIAL PRICES AND AVAILABILITY OF RAW MATERIALS COULD ADVERSELY AFFECT THE COMPANY'S BUSINESS.

The cost of raw materials is a major element of the total cost of many of the Company's products. For example, Filtertek's petroleum-based resins and the Test segment's critical components rely on purchases of raw materials from third parties. Increases in the prices of raw materials (such as steel, copper, nickel, zinc, wood and petrochemical products) could have an adverse impact on business by, among other things, increasing costs and reducing margins.

In addition, the Company's reliance on sole or limited sources of supply of raw materials in each of its segments could adversely affect the business. For example, there are a limited number of suppliers of Filtertek's petroleum-based raw materials. Certain refineries that produce these materials are concentrated in hurricane areas. Weather-created disruptions in supply, in addition to affecting costs, could impact the Company's ability to procure an adequate supply of these raw materials and delay or prevent deliveries of products to customers. Also, many petroleum supplies come from countries with unstable political environments. Supplies of base petroleum could be impacted by events such as embargoes and regional conflicts.

CHANGES IN TEST STANDARDS COULD ADVERSELY IMPACT TEST SEGMENT SALES

A significant portion of the Test segment's business involves sales to technology customers, which results from these customers needing to meet specific international and domestic test standards. If demand for product testing from these customers decreases, the Company's business could be adversely affected. Likewise, if regulatory agencies eliminate or reduce certain domestic or international test standards, the Company's sales could be adversely affected. For example, if it were determined that there is no need to include Wi-Fi technology in mobile phones, there may be no need for certain testing on mobile phones. Also, if a regulatory authority relaxes the test standards for certain electronic devices because they do not interfere with the broadcast spectrum, sales of certain Test products could be reduced.

DIMINISHING MARKET SHARE OF AUTOMOTIVE CUSTOMERS COULD AFFECT FILTRATION/FLUID FLOW SEGMENT SALES.

Filtertek relies heavily on sales of its products for use in the North American automotive industry. The North American automotive manufacturers are losing market share to foreign competition, most of which do not currently use Filtertek products. This loss of market share could reduce the number of products that Filtertek will sell.

ECONOMIC, POLITICAL AND OTHER RISKS OF THE COMPANY'S INTERNATIONAL OPERATIONS COULD ADVERSELY AFFECT BUSINESS

In fiscal 2006, approximately 22% of the Company's sales were made to international customers. An economic downturn or an adverse change in the political situation in certain foreign countries in which the Company does business could cause a decline in revenues and adversely affect the Company's financial condition. For example, the Test segment does significant business in Asia. Changes in the Asian political climate or political changes in specific Asian countries could negatively affect the Company's business. Filtertek has significant operations in Europe. Softness in the European economy could have a significant adverse effect on the Company's European revenues, which represented approximately 9% of the Company's total revenues in fiscal 2006.

The Company's international sales are also subject to other risks inherent in foreign commerce, including currency fluctuations and devaluations, the risk of war and terrorism, differences in foreign laws, uncertainties as to enforcement of contract rights, and difficulties in negotiating and resolving disputes with foreign customers.

SALES OF GOVERNMENT PRODUCTS DEPEND UPON CONTINUED GOVERNMENT FUNDING.

During the past three years, from 6% to 8% of the Company's revenues has been generated from sales to the U.S. Government or its contractors. These sales are dependent on continuous government funding of its programs. There could be reductions or terminations of the government funding on programs which are applicable to the Company or its customers. These funding effects could severely affect the Company's sales and profit, and could bring about a major restructuring of Company operations, which could result in an adverse effect on its financial results.

For example, a significant part of VACCO's sales involve major government defense and space programs. Government reduction in spending on these programs could have a significant adverse impact on Company financial results.

THE END OF CUSTOMER PRODUCT LIFE CYCLES COULD NEGATIVELY AFFECT FILTRATION/FLUID FLOW SEGMENT RESULTS.

Many of the Company's filtration products are sold to be components in the customers' end-products. If a customer discontinues a certain end-product line, the ability of the Company to continue to sell those components will be reduced or eliminated. The result could be a significant decrease in Company sales and revenue.

For example, a substantial portion of PTI's revenue is generated from commercial aviation aftermarket sales. As certain aircraft are retired and replaced by newer aircraft, there could be a corresponding decrease in sales and revenue associated with the Company's current products. Such a decrease could adversely affect the Company's operating results. In addition, if the Government cuts back the space program, VACCO's sales of space products would be reduced, and its revenues could be adversely affected. Further, if the market for large motor vehicles softens, the demand for Filtertek's automotive products will decline, which may cause an impact on revenues.

DISPUTES WITH CONTRACTORS COULD ADVERSELY AFFECT THE TEST SEGMENT'S COSTS.

A major portion of the Test segment's business involves working in conjunction with contractors to produce the end-product, such as an electronic test chamber. If there are performance problems caused by either the Company or a contractor, these often result in cost overruns and may lead to a dispute as to which party is responsible. The resolution of such disputes can result in arbitration or litigation, and could involve significant expense including attorneys' fees. In addition, these disputes may result in reduction in revenue or even a loss to the Company on a particular project.

ACQUISITIONS OF OTHER COMPANIES CARRY RISK.

Acquisitions of other companies involve numerous risks, including difficulties in the integration of the operations, technologies and products of the acquired companies, the potential exposure to unanticipated and undisclosed liabilities, the potential that expected benefits or synergies are not realized and that operating costs increase, the potential loss of key personnel, suppliers or customers of acquired businesses and the diversion of management's time and attention from other business concerns. Although management will attempt to evaluate the risks inherent in any particular transaction, no assurances can be made that the Company will properly ascertain all such risks.

DESPITE ITS EFFORTS, THE COMPANY MAY BE UNABLE TO ADEQUATELY PROTECT ITS INTELLECTUAL PROPERTY.

Despite the Company's efforts to protect its intellectual property, unauthorized parties or competitors may copy or otherwise obtain and use the Company's products and technology, particularly in foreign countries where the laws may not protect the Company's proprietary rights as fully as in the United States. Current and future actions to enforce the Company's proprietary rights may result in substantial costs and diversion of resources. No assurances can be made that any such actions will be successful. In addition, the Company may not elect to pursue an unauthorized user due to the high costs and uncertainties associated with litigation. The Company may also face exposure to claims by others challenging its intellectual property rights.

CHANGES IN ENVIRONMENTAL OR REGULATORY REQUIREMENTS COULD INCREASE EXPENSES AND ADVERSELY AFFECT PROFITABILITY.

The Company's operations and properties are subject to U.S. and foreign environmental laws and regulations governing, among other things, the generation, storage, emission, discharge, transportation, treatment and disposal of hazardous materials and the clean up of contaminated properties. Changes in such requirements could increase the cost of compliance. Failure to comply could result in the imposition of significant fines, suspension of production, alteration of product processes, cessation of operations or other actions, which could materially and adversely affect the Company's business, financial condition and results of operations.

COMPETITION IS BROADLY BASED AND GLOBAL IN SCOPE.

The Company faces competition from a large number of manufacturers and distributors for nearly all of its products. Some of the Company's competitors are larger, more diversified corporations with greater financial, marketing, production and research and development resources. If the Company cannot compete successfully against current or future competitors, it could have a material adverse effect on the Company's business, financial condition and results of operations.

FORWARD-LOOKING INFORMATION

Statements contained in this Form 10-K regarding future events and the Company's future results that are based on current expectations, estimates, forecasts and projections about the Company's performance and the industries in which the Company operates, the Company's ability to utilize NOLs, completion of backlog, adequacy of the Company's credit facility and future cash flows, estimates of anticipated contract costs and revenues, the timing, amount and success of claims for research credits, the success of software development efforts and resulting costs, acceptance by PG&E of the final version of DCSI's TNG software, growth in the AMR market, potential customer contracts, the anticipated value of the PG&E contracts, the outcome of current litigation, claims and charges, recoverability of deferred tax assets, continued reinvestment of foreign earnings, the impact of SFAS 158, future costs relating to environmental matters, share repurchases, investments, sustained performance improvement, performance improvement initiatives, growth opportunities, new product development, the Company's ability to increase stockholder value, acquisitions, and other statements contained herein which are not strictly historical are considered "forward-looking statements" within the meaning of the safe harbor provisions of the federal securities laws. Words such as expects, anticipates, targets, goals, projects, intends, plans, believes, estimates, variations of such words, and similar expressions are intended to identify such forward-looking statements. Investors are cautioned that such statements are only predictions, speak only as of the date of this report, and the Company undertakes no duty to update. The Company's actual results in the future may differ materially from those projected in the forward-looking statements due to risks and uncertainties that exist in the Company's operations and business environment including, but not limited to: those described in this Item 1A. Risk Factors; actions by the California Public Utility Commission; PG&E's Board of Directors or PG&E's management impacting PG&E's AMI projects; the timing and success of DCSI's software development efforts; the timing and content of purchase order releases under the PG&E contracts; and DCSI's and Hexagram's successful performance of the PG&E contracts; the timing and execution of real estate sales; termination for convenience of customer contracts; timing and magnitude of future contract awards; weakening of economic conditions in served markets; the success of the Company's competitors; changes in customer demands or customer insolvencies; competition; intellectual property rights; technical difficulties; the availability of selected acquisitions; the timing, pricing and availability of shares offered for sale; delivery delays or defaults by customers; performance issues with key customers, suppliers and subcontractors; material changes in the costs of certain raw materials; the successful sale of the Company's Puerto Rico facility; collective bargaining and labor disputes; changes in laws and regulations including but not limited to changes in accounting standards and taxation requirements; costs relating to environmental matters; litigation uncertainty; and the Company's successful execution of internal operating plans.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

The Company's principal buildings contain approximately 1,258,450 square feet of floor space. Approximately 737,300 square feet are owned by the Company and approximately 521,150 square feet are leased. See Note 8 of the Notes to Consolidated Financial Statements in the 2006 Annual Report, which information is herein incorporated by reference. The principal plants and offices are as follows*:

Location	Size (Sq. Ft.)	Sq. Ft. Owned/Leased	Lease Expiration Date	Principal Use (Operating Segment)
South El Monte, CA	132,100	Owned-100,100 Leased — 32,000	1-2-2008	Management, Engineering and Manufacturing (Filtration/Fluid Flow)
Oxnard, CA	127,400	Owned		Management, Engineering and Manufacturing (Filtration/Fluid Flow)
Hebron, IL	104,200	Owned		Management, Engineering and Manufacturing (Filtration/Fluid Flow)
Durant, OK	100,000	Owned		Manufacturing (Test)
St. Louis, MO	91,800	Leased	3-31-2008 (two 5-year renewal options)	Management and Engineering (Communications)
Huntley, IL	85,000	Owned		Manufacturing (Filtration/Fluid Flow)

Location	Size (Sq. Ft.)	Sq. Ft. Owned/Leased	Lease Expiration Date	Principal Use (Operating Segment)
Austin, TX	75,200	Leased	12-31-2007 (two 5-year renewal options)	Management, Engineering and Manufacturing (Test)
Cedar Park, TX	70,000	Owned		Management, Engineering and Manufacturing (Test)
Cleveland, OH	59,600	Leased	1-31-2011 (four 3-year renewal options)	Management, Engineering and Manufacturing (Communications)
Glendale Heights, IL	59,400	Leased	3-31-2010 (three 3-year renewal options)	Management, Engineering and Manufacturing (Test)
Sao Paulo, Brazil	52,500	Leased	7-31-2007	Manufacturing (Filtration/Fluid Flow)
Eura, Finland	40,900	Owned		Management, Engineering and Manufacturing (Test)
Newcastle West, Ireland	37,500	Owned		Manufacturing (Filtration/Fluid Flow)
Plailly, France	37,200	Owned		Engineering and Manufacturing (Filtration/Fluid Flow)
St. Louis, MO	35,000	Owned		Management and Engineering(Communications)
Juarez, Mexico	34,400	Leased	12-31-2007	Engineering and Manufacturing (Filtration/Fluid Flow)
Minocqua, WI	30,200	Leased	3-31-2010 (three 3-year renewal options)	Engineering and Manufacturing (Test)
Beijing, China	26,200	Leased	4,600 sq. ft. Office 8-30-2007. 21,700 sq. ft. Plant 12-31-2006	Manufacturing (Test)
Stevenage, England	25,650	Leased	8-11-2017 (option to terminate on 8-12-2007)	Management, Engineering and Manufacturing (Test)
St. Louis, MO	19,000	Leased	8-31-2015 (one 5-year renewal option)	ESCO Headquarters
Wellesley, MA	15,100	Leased	9-30-2012	Management and Engineering (Communications)

* The table does not include an owned vacant facility in Patillas, Puerto Rico, consisting of approximately 110,000 square feet, that was formerly used as a Filtration/Fluid Flow manufacturing facility. The Company ceased operations in this facility in March 2004, and is currently marketing it for sale.

The Company believes its buildings, machinery and equipment have been generally well maintained, are in good operating condition and are adequate for the Company's current production requirements.

Item 3. Legal Proceedings

As a normal incident of the businesses in which the Company is engaged, various claims, charges and litigation are asserted or commenced from time to time against the Company. Lindgren is arbitrating a contract dispute with a prime contractor involving the assertion of certain construction delay damages of approximately $3.7 million. The project was completed in 2005. Lindgren vigorously denies responsibility for this delay and for these damages, and has asserted a claim against the prime contractor of $0.9 million based on damages suffered by Lindgren. Lindgren continues to aggressively defend its position and pursue its right to affirmative damages; however, there can be no assurance of the outcome at this time. With respect to claims and litigation asserted or commenced against the Company, it is the opinion of management, that final judgments, if any, which might be rendered against the Company are adequately reserved, covered by insurance and are not likely to have a material adverse effect on its financial condition or results of operation

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

None.

Executive Officers of the Registrant

The following sets forth certain information as of December 13, 2006 with respect to ESCO's executive officers. These officers have been elected to terms which expire at the first meeting of the Board of Directors after the next annual meeting of Stockholders.

Name	Age	Position(s)
Victor L. Richey, Jr.*	49	Chairman, President, Chief Executive Officer and Director
Gary E. Muenster	46	Senior Vice President and Chief Financial Officer
Alyson S. Barclay	47	Vice President, Secretary and General Counsel

* Also Chairman of the Executive Committee of the Board of Directors.

There are no family relationships among any of the executive officers and directors.

Mr. Richey was President and Chief Operating Officer of ESCO from August 2001 until October 2002. Since October 2002, he has been Chief Executive Officer, and since April 2003, he has also been Chairman. Since October 2006, he has also been President.

Mr. Muenster was Vice President and Controller of ESCO from May 1998 until October 2002. He was Vice President and Chief Financial Officer from October 2002 until November 2005. Since the latter date, he has been Senior Vice President and Chief Financial Officer.

Ms. Barclay has been Vice President, Secretary and General Counsel of ESCO since October 1999.

PART II

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

The information required by this item is incorporated herein by reference to Notes 11 and 12 of the Notes to Consolidated Financial Statements, "Common Stock Market Price" and "Shareholders' Summary—Capital Stock Information" appearing in the 2006 Annual Report. As of December 6, 2006, there were approximately 1,815 registered holders of Common Stock (not including Company employees holding shares under the Employee Stock Purchase Plan). ESCO does not anticipate, currently or in the foreseeable future, paying cash dividends on the Common Stock, although it reserves the right to do so to the extent permitted by applicable law and agreements. ESCO's dividend policy will be reviewed by the Board of Directors at such future time as may be appropriate in light of relevant factors at that time, based on ESCO's earnings and financial position and such other business considerations as the Board deems relevant. See Item 12 for equity compensation plan information.

ISSUER PURCHASES OF EQUITY SECURITIES*:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
July 1-31, 2006	0	N.A.	0	0
August 1-31, 2006	0	N.A.	0	0
Sep. 1-30, 2006	0	N.A.	0	0
Total	0	N.A.	0	1,200,000

* A common stock repurchase program (the "2001 Program") was first approved by the Company's Board of Directors on February 8, 2001 for a maximum of 2,600,000 shares. On August 7, 2003, this program was extended to September 30, 2004. On August 10, 2004, it was announced that the program was extended to September 30, 2006. On August 3, 2006, the Board of Directors cancelled the 2001 Program, and replaced it with a new common stock repurchase program (the "2006 Program") for a maximum of 1,200,000 shares. The 2006 Program will expire September 30, 2008. There currently is no repurchase program which the Company has determined to terminate prior to expiration, or under which the Company does not intend to make further purchases.

Item 6. Selected Financial Data

The information required by this item is incorporated herein by reference to "Five-Year Financial Summary" and Notes 2 and 3 of the Notes to Consolidated Financial Statements appearing in the 2006 Annual Report.

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

The information required by this item is incorporated herein by reference to "Management's Discussion and Analysis" appearing in the 2006 Annual Report.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The information required by this item is incorporated herein by reference to "Management's Discussion and Analysis — Market Risk Analysis" appearing in the 2006 Annual Report.

Item 8. Financial Statements and Supplementary Data

The information required by this item is incorporated herein by reference to the Consolidated Financial Statements of the Company on pages 25 through 45 and the report thereon of KPMG LLP, an independent registered public accounting firm, appearing on page 48 of the 2006 Annual Report.

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

None.

Item 9A. Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as defined in Rules 13A-15(e) and 15d—15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act") as of September 30, 2006. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in Company reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Management's Report on Internal Control Over Financial Reporting and the attestation report thereon of KPMG LLP are incorporated herein by reference to pages 47 and 49, respectively, in the 2006 Annual Report.

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the fiscal quarter ended September 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

Information regarding nominees and directors appearing under "Nominees and Continuing Directors" in the 2007 Proxy Statement is hereby incorporated by reference. Information regarding executive officers is set forth in Part I of this Form 10-K. Information regarding the Audit and Finance Committee and its members appearing under "Board of Directors and Committees" in the 2007 Proxy Statement is hereby incorporated by reference.

Information appearing under "Section 16(a) Beneficial Ownership Reporting Compliance" in the 2007 Proxy Statement is hereby incorporated by reference.

The Company has adopted codes of ethics which apply to its chief executive officer, its chief financial officer and all other senior executives, as well as all Company employees. The following documents are available free of charge through the Company's internet website at www.escotechnologies.com and in print to any person who requests them: Corporate Governance Guidelines; Charters of the Audit and Finance Committee, Human Resources and Compensation Committee, and Nominating and Corporate Governance Committee; Code of Business Conduct and Ethics; and Code of Ethics for Senior Financial Officers.

Item 11. Executive Compensation

Information appearing under "Board of Directors and Committees" and "Executive Compensation" (except for the "Report of the Human Resources And Compensation Committee On Executive Compensation" and the "Performance Graph") in the 2007 Proxy Statement is hereby incorporated by reference.

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

The information regarding beneficial ownership of shares of common stock by nominees and directors, by executive officers, by directors and executive officers as a group and by any known five percent stockholders appearing under "Security Ownership of Directors and Executive Officers" and "Security Ownership of Certain Beneficial Owners" in the 2007 Proxy Statement is hereby incorporated by reference.

Equity Compensation Plan Information:

The following table summarizes certain information regarding Common Shares that may be issued by the Company pursuant to its equity compensation plans existing as of September 30, 2006.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights(1)	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))(1)
	(a)	(b)	(c)
Equity compensation plans approved by security holders (2)	1,543,078(3)	$26.6004(4)	2,076,773(5)(6)
Equity compensation plans not approved by security holders	0	N/A	278,758(7)
Total	1,543,078	$26.6004	2,355,531

(1) Number of Common Shares is subject to adjustment for any future changes in capitalization for stock splits, stock dividends and similar events.

(2) Consists of the Company's 1990, 1994 and 1999 Stock Option Plans, the 2001 Stock Incentive Plan and the 2004 Incentive Compensation Plan. Each of the above-cited Plans has been amended without Stockholder approval in accordance with its terms, as follows: the Company's 1990, 1994 and 1999 Stock Option Plans have been amended to provide for tax withholding, to provide for adjustment upon a special distribution and in certain other respects; the 1994 and 1999 Stock Option Plans have been amended to reflect the change of the Company's name and the elimination of the Company's common stock trust receipts; the 1994 Stock Option Plan was amended to authorize the Human Resources and Compensation Committee (the "Committee"), in its discretion, to: (i) permit an optionee who terminates employment with the approval of the Company to exercise his stock option at any time within three months after termination, but before ten years from the date of grant, and (ii) direct that an option award agreement may permit an optionee who terminates employment on account of retirement on or after age 60 to exercise his stock option up to five years after retirement, but before ten years from the date of grant; the 1990, 1994 and 1999 Stock Option Plans and the 2001 Stock Incentive Plan were amended to authorize the Committee to delegate to any employee the power to extend a stock option beyond termination of employment for persons who are not "officers" as defined in Rule 16a-1 under the Exchange Act; the 1994 and 1999 Stock Option Plans and the 2001 Stock Incentive Plan have been amended to authorize the Committee to delegate to the Chief Executive Officer the power to grant stock options to persons who are not such "officers", with the limitation of 10,000 shares per award and 100,000 shares awarded in the aggregate in any fiscal year; the 2001 Stock Incentive Plan and the 2004 Incentive Compensation Plan were amended with respect to Performance Share distributions to: (i) eliminate the participant's option to pay cash for tax withholding and receive all shares due, and (ii) eliminate the participant's option to defer the distribution; and the 2004 Incentive Compensation Plan was amended with respect to Performance Share distributions to eliminate the Committee's discretion to determine the percentage of the distribution to be made in shares or to be withheld for tax payments.

(3) Includes 155,730 Common Shares issuable in connection with the vesting and distribution of outstanding performance-accelerated restricted share awards under the Company's 2001 Stock Incentive Plan.

(4) Does not include 155,730 Common Shares issuable in connection with the vesting and distribution of outstanding performance-accelerated restricted share awards under the 2001 Stock Incentive Plan, for which there are no exercise prices.

(5) Comprises 15,475 Common Shares under the 1999 Stock Option Plan, 334,178 Common Shares under the 2001 Stock Incentive Plan and 1,227,120 Common Shares under the 2004 Incentive Compensation Plan.

(6) Does not include shares that may be purchased on the open market pursuant to the Company's Employee Stock Purchase Plan (the "ESPP"). Under the ESPP, participants may elect to have up to 10% of their current salary or wages withheld and contributed to one or more independent trustees for the purchase of Common Shares. At the discretion of an officer of the Company, the Company or a domestic subsidiary or division may contribute cash in an amount not to exceed 20% of the amounts contributed by participants. The total number of Common Shares purchased with the Company's matching contributions, however, may not exceed 183,446. As of September 30, 2006, 25,310 shares had been purchased with the Company's matching funds.

(7) Represents Common Shares issuable pursuant to the Compensation Plan for Non-Employee Directors (the "Compensation Plan"), which provides for each director to be paid (in addition to other fees) an annual retainer fee payable partially in cash and partially in Common Shares. Periodically, the Human Resources and Compensation Committee of the Board of Directors determines the amount of the retainer fee and the allocation of the fee between cash and Common Shares. The maximum number of Common Shares available for distribution under the Compensation Plan is 400,000 shares. The stock portion of the retainer fee is distributable in quarterly installments. Directors may elect to defer receipt of all of their cash compensation and/or all of the stock portion of the retainer fee. The deferred amounts are credited to the director's deferred compensation account in stock equivalents. Deferred amounts are distributed in Common Shares or cash at such future dates as specified by the director unless distribution is accelerated in certain circumstances, including a change in control of the Company. The stock portion which has been deferred may only be distributed in Common Shares.

Item 13. Certain Relationships and Related Transactions

None.

Item 14. Principal Accounting Fees and Services

Information regarding the Company's independent auditors, their fees and services, and the Company's Audit and Finance Committee's pre-approval policies and procedures regarding such fees and services appearing under "III. Independent Auditors" in the 2007 Proxy Statement is hereby incorporated by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) Documents filed as a part of this report:

1. The Consolidated Financial Statements of the Company on pages 25 through 45 and the Report of Independent Registered Public Accounting Firm thereon of KPMG LLP appearing on page 48 of the 2006 Annual Report.
2. Financial statement schedules have been omitted because the subject matter is disclosed elsewhere in the financial statements and notes thereto, not required or not applicable, or the amounts are not sufficient to require submission.

Table of Contents

3. Exhibits:

Exhibit Number	Description	Filed Herewith or Incorporated by Reference to Document Indicated By Footnote
3.1	Restated Articles of Incorporation	Incorporated by Reference, Exhibit 3(a)[1]
3.2	Amended Certificate of Designation, Preferences and Rights of Series A Participating Cumulative Preferred Stock of the Registrant	Incorporated by Reference, Exhibit 4(e)[2]
3.3	Articles of Merger effective July 10, 2000	Incorporated by Reference, Exhibit 3(c)[3]
3.4	Bylaws, as amended and restated	Incorporated by Reference, Exhibit 3.4[4]
4.1	Specimen Common Stock Certificate	Incorporated by Reference, Exhibit 4(a)[3]
4.2	Specimen Rights Certificate	Incorporated by Reference, Exhibit B to Exhibit 4.1[5]
4.3	Rights Agreement dated as of September 24, 1990 (as amended and restated as of February 3, 2000) between the Registrant and Registrar and Transfer Company, as successor Rights Agent	Incorporated by Reference, Exhibit 4.1[5]
4.4	Credit Agreement dated as of October 6, 2004, among the Registrant, Wells Fargo Bank, N.A., as agent, and the lenders listed therein	Incorporated by Reference, Exhibit 4.4[6]
10.1	Form of Indemnification Agreement with each of ESCO's directors.	Incorporated by Reference, Exhibit 10(k)[7]
10.2	Supplemental Executive Retirement Plan as amended and restated as of August 2, 1993*	Incorporated by Reference, Exhibit 10(n)[8]
10.3	Second Amendment to Supplemental Executive Retirement Plan effective May 1, 2001*	Incorporated by Reference, Exhibit 10.4[9]
10.4	Directors' Extended Compensation Plan*	Incorporated by Reference, Exhibit 10(o)[8]
10.5	First Amendment to Directors' Extended Compensation Plan effective January 1, 2000*	Incorporated by Reference, Exhibit 10.11[10]

10.6	Second Amendment to Directors' Extended Compensation Plan effective April 1, 2001*	Incorporated by Reference, Exhibit 10.7[9]
10.7	1994 Stock Option Plan (as amended and restated effective October 16, 2000)*	Incorporated by Reference, Exhibit 10.1[11]
10.8	Amendment to 1994 Stock Option Plan effective July 18, 2002*	Incorporated by Reference, Exhibit 10(b)[12]
10.9	Form of Incentive Stock Option Agreement*	Incorporated by Reference, Exhibit 10.15[10]
10.10	Severance Plan adopted as of August 10, 1995 (as restated February 5, 2002)*	Incorporated by Reference, Exhibit 10[13]
10.11	Amendment to 1994 Stock Option Plan effective August 7, 2003*	Incorporated by Reference, Exhibit 10.12[4]
10.12	1999 Stock Option Plan (as amended and restated effective October 16, 2000)*	Incorporated by Reference, Exhibit 10.2[11]
10.13	Form of Incentive Stock Option Agreement*	Incorporated by Reference, Exhibit 10.3[11]
10.14	Amendment to 1999 Stock Option Plan effective August 7, 2003*	Incorporated by Reference, Exhibit 10.15[4]
10.15	Employment Agreement with Executive Officer*[14]	Incorporated by Reference, Exhibit 10(bb)[1]
10.16	Amendment to Employment Agreement with Executive Officer*[15]	Incorporated by Reference, Exhibit 10.18[9]
10.17	Executive Stock Purchase Plan*	Incorporated by Reference, Exhibit 10.24[10]
10.18	Compensation Plan For Non-Employee Directors*	Incorporated by Reference, Exhibit 10.22[9]
10.19	2001 Stock Incentive Plan*	Incorporated by Reference, Exhibit B[16]
10.20	Form of Incentive Stock Option Agreement*	Incorporated by Reference, Exhibit 10.24[17]
10.21	Form of Non-qualified Stock Option Agreement*	Incorporated by Reference, Exhibit 10.25[17]
10.22	Form of Notice of Award—Performance— Accelerated Restricted Stock *	Incorporated by Reference, Exhibit 10.26[17]
10.23	Form of Supplemental Executive Retirement Plan Agreement *	Incorporated by Reference, Exhibit 10.28[17]
10.24	Amendment to 2001 Stock Incentive Plan effective August 7, 2003*	Incorporated by Reference, Exhibit 10.29[4]

10.25	Sixth Amendment and Restatement of Employee Stock Purchase Plan effective as of October 15, 2003*	Incorporated by Reference, Appendix C[18]
10.26	Second Amendment to Employment Agreement with V.L. Richey, Jr. (identical document with C.J. Kretschmer)*	Incorporated by Reference, Exhibit 10.1[19]
10.27	Second Amendment to Employment Agreement with G.E. Muenster (identical document with A.S. Barclay)*	Incorporated by Reference, Exhibit 10.2[19]
10.28	Notice of Award — restricted stock award to V.L. Richey, Jr. (identical documents except for number of shares awarded for: C.J. Kretschmer — 4,750 shares; G.E. Muenster — 2,400 shares; A.S. Barclay — 1,800 shares)*	Incorporated by Reference, Exhibit 10.3[19]
10.29	2004 Incentive Compensation Plan*	Incorporated by Reference, Appendix B[18]
10.30	Summary of Non-Employee Directors' Compensation*	Incorporated by Reference, Exhibit 10.1[20]
10.31	Performance Compensation Plan Amended and Restated as of November 25, 2002*	Incorporated by Reference, Exhibit 10.2[20]
10.32	2005 Performance Measures and Evaluation Criteria under Performance Compensation Plan*	Incorporated by Reference, Exhibit 10.3[20]
10.33	Awards to Executive Officers Not Reported on Form 8-K, October 4, 2004*	Incorporated by Reference, Exhibit 10.4[20]
10.34	Form of Notice of Award-Performance-Accelerated Restricted-Stock under 2001 Stock Incentive Plan*	Incorporated by Reference, Exhibit 10.5[20]
10.35	Form of Incentive Stock Option Agreement under 2004 Incentive Compensation Plan*	Incorporated by Reference, Exhibit 10.6[20]
10.36	Form of Nonqualified Stock Option Agreement under 2004 Incentive Compensation Plan*	Incorporated by Reference, Exhibit 10.7[20]
10.37	Form of Incentive Stock Option Agreement under 2001 Stock Incentive Plan*	Incorporated by Reference, Exhibit 10.8[20]
10.38	Form of Nonqualified Stock Option Agreement under 2001 Stock Incentive Plan*	Incorporated by Reference, Exhibit 10.9[20]
10.39	Second Amendment to 2001 Stock Incentive Plan effective August 3, 2006*	
10.40	First Amendment to 2004 Incentive Compensation Plan effective August 3, 2006*	
10.41	Employment Agreement with C.J. Kretschmer effective October 1, 2006*	

13	The following-listed sections of the Annual Report to Stockholders for the year ended September 30, 2006: - Five-Year Financial Summary (p. 50) - Management's Discussion and Analysis (pgs. 13-24) - Consolidated Financial Statements (pgs. 25-45) and Report of Independent Registered Public Accounting Firm (p. 48) - Management's Report on Internal Control over Financial Reporting (p.47) - Report of Independent Registered Public Accounting Firm (p.49) - Shareholders' Summary—Capital Stock Information (p. 51) - Common Stock Market Price (p. 50)
21	Subsidiaries of ESCO
23	Consent of Independent Registered Public Accounting Firm
31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32	Certification of Chief Executive Officer and Chief Financial Officer

[1] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 1999, at the Exhibit indicated.

[2] Incorporated by reference to Form 10-Q for the fiscal quarter ended March 31, 2000, at the Exhibit indicated.

[3] Incorporated by reference to Form 10-Q for the fiscal quarter ended June 30, 2000, at the Exhibit indicated.

[4] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 2003, at the Exhibit indicated.

[5] Incorporated by reference to Current Report on Form 8-K dated February 3, 2000, at the Exhibit indicated.

[6] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 2004, at the Exhibit indicated.

[7] Incorporated by reference to Form l0-K for the fiscal year ended September 30, l991, at the Exhibit indicated.

[8] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 1993, at the Exhibit indicated.

[9] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 2001, at the Exhibit indicated.

[10] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 2000, at the

Exhibit indicated.

[11] Incorporated by reference to Form 10-Q for the fiscal quarter ended December 31, 2000, at the Exhibit indicated.

[12] Incorporated by reference to Form 10-Q for the fiscal quarter ended June 30, 2002, at the Exhibit indicated.

[13] Incorporated by reference to Form 10-Q for the fiscal quarter ended March 31, 2002, at the Exhibit indicated.

[14] Identical Employment Agreements between ESCO and executive officers A.S. Barclay, G.E. Muenster and V.L. Richey, Jr., except that in the cases of Ms. Barclay and Mr. Muenster the minimum annual salary is $94,000 and $108,000, respectively.

[15] Identical Amendments to Employment Agreements between ESCO and executive officers A.S. Barclay, G.E. Muenster and V.L. Richey, Jr.

[16] Incorporated by reference to Notice of Annual Meeting of the Stockholders and Proxy Statement dated December 11, 2000, at the Exhibit indicated.

[17] Incorporated by reference to Form 10-K for the fiscal year ended September 30, 2002, at the Exhibit indicated.

[18] Incorporated by reference to Notice of Annual Meeting of the Stockholders and Proxy Statement dated December 29, 2003, at the Appendix indicated.

[19] Incorporated by reference to Form 10-Q for the fiscal quarter ended June 30, 2004, at the Exhibit indicated.

[20] Incorporated by reference to Form 10-Q for the fiscal quarter ended December 31, 2004, at the Exhibit indicated.

* Represents a management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K pursuant to Item 15(c) of this Part IV.

NOTE: C.J. Kretschmer’s participation in the Severance Plan (Exhibit No. 10.10), his Employment Agreement, as amended, (Exhibit Nos. 10.15, 10.16 and 10.26) and his restricted stock award (Exhibit 10.33) were terminated and/or cancelled effective September 30, 2006.

(b) Exhibits: Reference is made to the list of exhibits in this Part IV, Item 15(a)3 above.

(c) Financial Statement Schedules: Reference is made to Part IV, Item 15(a)2 above.

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.

ESCO TECHNOLOGIES INC.

Date: December 13, 2006

By /s/ V.L. Richey, Jr.
V.L. Richey, Jr.
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below effective December 13, 2006, by the following persons on behalf of the registrant and in the capacities indicated.

SIGNATURE	TITLE
/s/ V.L. Richey, Jr. V.L. Richey, Jr.	Chairman, President, Chief Executive Officer and Director
/s/ G.E. Muenster G.E. Muenster	Senior Vice President and Chief Financial Officer, Principal Accounting Officer
W.S. Antle III	Director
/s/ J.M. McConnell J.M. McConnell	Director
/s/ L.W. Solley L.W. Solley	Director
/s/ J.M. Stolze J.M. Stolze	Director
/s/ D.C. Trauscht D.C. Trauscht	Director
J.D. Woods	Director

Table of Contents

INDEX TO EXHIBITS

Exhibits are listed by numbers corresponding to the Exhibit Table of Item 601 in Regulation S-K.

Exhibit No.	Exhibit
10.39	Second Amendment to 2001 Stock Incentive Plan effective August 3, 2006
10.40	First Amendment to 2004 Incentive Compensation Plan effective August 3, 2006
10.41	Employment Agreement with C.J. Kretschmer effective October 1, 2006
13	The following-listed sections of the Annual Report to Stockholders for the year ended September 30, 2006: • Five-year Financial Summary (p. 50) • Management's Discussion and Analysis (pgs. 13-24) • Consolidated Financial Statements (pgs. 25-45) and Report of Independent Registered Public Accounting Firm (p. 48) • Management's Report on Internal Control over Financial Reporting (p. 47) • Report of Independent Registered Public Accounting Firm (p.49) • Shareholders' Summary—Capital Stock Information (p. 51) • Common Stock Market Price (p. 50)
21	Subsidiaries of ESCO
23	Consent of Independent Registered Public Accounting Firm
31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32	Certification of Chief Executive Officer and Chief Financial Officer

See Item 15(a)3 for a list of exhibits incorporated by reference

EXHIBIT: 10.39

**SECOND AMENDMENT TO THE ESCO TECHNOLOGIES INC.
2001 STOCK INCENTIVE PLAN**

WHEREAS, ESCO Technologies Inc. (“Company”) adopted the ESCO Technologies Inc. 2001 Stock Incentive Plan (“Plan”) for the benefits of eligible employees; and

WHEREAS, the Company retained the right to amend the Plan pursuant to Section 13 thereof; and

WHEREAS, the Company desires to amend the Plan effective as of August 3, 2006:

NOW, THEREFORE, effective as of August 3, 2006, the Plan is amended as follows:

1. The following is added at the end of section 11(iv):

Provided, however, that the previous sentence shall not apply to the distribution under a Performance Share Award.

2. Section 9(d) is deleted in its entirety and Sections 9(e)-9(g) are renumbered Sections 9(d)-9(f) respectively.

IN WITNESS WHEREOF, the foregoing Amendment was adopted on the 3rd day of August, 2006.

EXHIBIT 10.40

**FIRST AMENDMENT TO THE ESCO TECHNOLOGIES INC.
2004 INCENTIVE COMPENSATION PLAN**

WHEREAS, ESCO Technologies Inc. ("Company") adopted the ESCO Technologies Inc. 2004 Incentive Compensation Plan ("Plan") for the benefits of eligible employees; and

WHEREAS, the Company retained the right to amend the Plan pursuant to Section 15 thereof; and

WHEREAS, the Company desires to amend the Plan effective as of August 3, 2006:

NOW, THEREFORE, effective as of August 3, 2006, the Plan is amended as follows:

1. The last two sentences of section 9(c) are deleted.

2. . Section 9(d) is deleted in its entirety and Sections 9(e) and 9(f) are renumbered Sections 9(d) and 9(e) respectively.

3. The following is added at the end of Section 13(d):

Provided, however, that the previous sentence shall not apply to the distribution under a Performance Share Award.

IN WITNESS WHEREOF, the foregoing Amendment was adopted on the 3rd day of August, 2006.

EXHIBIT: 10.41

August 3, 2006

Mr. Charles J. Kretschmer
President & Chief Operating Officer
ESCO Technologies Inc.
9900A Clayton Road
St. Louis, MO 63124

Dear Chuck,

With regard to your letter of resignation dated August 3, 2006, the following provisions have been mutually agreed to:

1. Your current compensation, benefits and all agreements between you and ESCO shall remain in effect through September 30, 2006, the effective date of your resignation as President and Chief Operating Officer of ESCO.

2. Effective October 1, 2006 and for the duration of your employment with ESCO:

    a. You are appointed Vice President of ESCO, as an "at will" employee. Your salary shall be $250,000 per year. You are not guaranteed any performance compensation (bonus), except that you will be entitled to receive a bonus for fiscal year 2006 which is consistent with those paid to the Executive Officers, pursuant to ESCO's standard practice.

    b. You are not guaranteed the right to receive any stock option awards, performance-accelerated restricted stock awards, restricted stock awards or any other similar awards.

    c. You will continue to receive a car allowance of $1,500 per month, the current allowances attributable to your country club membership and financial planning, in addition to standard ESCO employee benefits.

    d. Stock option awards granted to you prior to the date hereof shall remain in full force and effect.

    e. The Performance-Accelerated Restricted Stock Award of 9,500 (post stock-split) ESCO shares, dated May 4, 2004 (scheduled to be paid out on March 31, 2007 contingent on your continued employment with ESCO), shall remain in full force and effect. However, any and all other Performance-Accelerated Restricted Stock Awards granted to you at any time are hereby terminated and are null and void.

f. Your primary duties shall include:

- Acquisition / divestiture activity
- Contract Manufacturing for the Communications Segment
- Selected major contract negotiations
- Profit improvement initiatives
- Other tasks as assigned

3. The above agreements are made in mutual consideration of each other and your “at will” employment with ESCO as stated above.

Chuck, please indicate your agreement to the foregoing by signing and returning the attached copy of this letter.

Sincerely,

ESCO Technologies Inc.

/s/ Victor L. Richey, Jr
Victor L. Richey, Jr.
Chairman and Chief Executive Officer

Agreed:

/s/ Charles J. Kretschmer
Charles J. Kretschmer

Date: 8-5-06

Exhibit 13

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto. The years 2006, 2005 and 2004 represent the fiscal years ended September 30, 2006, 2005 and 2004, respectively, and are used throughout the document. During 2005, the Company had a 2-for-1 stock split which was effected as a 100 percent stock dividend and was paid on September 23, 2005 to shareholders of record as of September 9, 2005. The 2004 common stock and per share amounts have been adjusted to reflect the stock split.

INTRODUCTION

ESCO Technologies Inc. and its wholly owned subsidiaries (ESCO, the Company) are organized into three reporting units: Communications, Filtration/Fluid Flow, and RF Shielding and Test (Test). The Company's business segments are comprised of the following primary operating entities:

- - Communications: Distribution Control Systems, Inc. (DCSI), Hexagram, Inc. (Hexagram), Nexus Energy Software, Inc. (Nexus), and Comtrak Technologies, L.L.C. (Comtrak),

- - Filtration/Fluid Flow: PTI Technologies Inc. (PTI), VACCO Industries (VACCO), and the Filtertek companies (Filtertek),

- - Test: EMC Group companies consisting primarily of ETS-Lindgren L.P. (ETS) and Lindgren RF Enclosures, Inc. (Lindgren).

The Communications unit is a proven supplier of special purpose fixed network communications systems for electric, gas and water utilities, including hardware and software to support advanced metering applications. DCSI's Two-Way Automatic Communications System, known as TWACS(R), is currently used for automatic meter reading (AMR) and related advanced metering functions serving approximately 200 utilities, as well as having load management capabilities. Hexagram's STAR(R) system, the premier wireless Advanced Metering Infrastructure (AMI), delivers two-way and one-way operation on secure licensed radio frequencies for more than 100 utilities serving electric, gas and water customers. Nexus provides best-in-class information solutions to more than 85 leading energy companies that add value to existing billing and metering infrastructure to allow both the utilities and their customers to better manage energy-driven transactions and decision making. Comtrak's SecurVision(R) product line provides digital video surveillance and security functions for large commercial enterprises and alarm monitoring companies. The Filtration/Fluid Flow unit develops, manufactures and markets a broad range of filtration products used in the purification and processing of liquids and gases. These engineered filtration products utilize membrane, precision screen and other technologies to protect critical processes and equipment from contaminants. Major applications include the removal of contaminants in fuel, lubrication and hydraulic systems, various health care applications, industrial processing, satellite propulsion systems, and oil processing. The Test unit is the industry leader in providing its customers with the ability to identify, measure and contain magnetic, electromagnetic and acoustic energy.

The divestiture of the Microfiltration and Separations businesses (MicroSep) was completed during the third quarter of fiscal 2004. The MicroSep businesses (previously included in the Filtration/Fluid Flow segment) included PTI Advanced Filtration Inc. (PTA), PTI Technologies Limited (PTL) and PTI S.p.A. (PTB). The MicroSep businesses are accounted for as "discontinued operations" in fiscal 2004.

ESCO continues to operate with meaningful growth prospects in its primary served markets and with considerable financial flexibility. The Company continues to focus on new products that incorporate proprietary design and process technologies. Management is committed to delivering shareholder value through internal growth, ongoing performance improvement initiatives, and selective acquisitions.

HIGHLIGHTS OF 2006 OPERATIONS

- - Sales, net earnings and earnings per share were $458.9 million, $31.3 million and $1.19 per share, respectively.

- - Net cash provided by operating activities was $58.6 million.

- - At September 30, 2006, cash on hand was $36.8 million with no debt outstanding.

- - The Company acquired Hexagram and Nexus for approximately $92 million in cash.

- - DCSI's AMR product sales to TXU Electric Delivery Company (TXU) increased to $27.1 million in 2006 from $7.2 million in 2005.

- - In November 2005, DCSI and Hexagram signed agreements to deliver AMI equipment, software and services to Pacific Gas & Electric Company (PG&E) for approximately nine million electric and gas customers over a five year deployment period beginning in 2007. The total anticipated contract value is expected to be up to approximately $535 million assuming full deployment.

- - Successful deployment of upgraded TWACS system software called "TNG" Versions 1.5 through 1.6.2 at PG&E.

RESULTS OF OPERATIONS

The following discussion refers to the Company's results from continuing operations, except where noted. The MicroSep businesses are accounted for as discontinued operations in 2004 in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Accordingly, amounts in the financial statements and related notes for 2004 presented reflect discontinued operations.

ACQUISITIONS

Effective February 1, 2006, the Company acquired the capital stock of Hexagram for a purchase price of approximately $66 million. The acquisition agreement also provides for contingent consideration of up to $6.3 million over a five year period following the acquisition if Hexagram exceeds certain sales targets. Hexagram is a radio-frequency (RF) fixed network AMR company headquartered in Cleveland, Ohio. Hexagram broadens the Company's served market and provides an RF based AMI system serving primarily gas and water utilities. Hexagram's annual revenue over the past three years has been in the range of $20 million to $35 million. The operating results for Hexagram, since the date of acquisition, are included within the Communications unit. The Company recorded approximately $51 million of goodwill and $3.5 million of trademarks as a result of the transaction. The Company also recorded $6.6 million of identifiable intangible assets consisting primarily of patents and proprietary know-how, customer contracts, and order backlog which are being amortized on a straight-line basis over periods ranging from six months to seven years.

Effective November 29, 2005, the Company acquired Nexus through an all cash for shares merger transaction for approximately $29 million in cash plus contingent cash consideration over the four year period following the merger if Nexus exceeds certain sales targets. Nexus is a software company headquartered in Wellesley, Massachusetts with annual revenues of approximately $10 million. Nexus broadens the Company's served market and provides software solutions that allow utilities to fully utilize the information produced by the Company's AMI systems. The operating results for Nexus, since the date of acquisition, are included within the Communications unit. The Company recorded approximately $24 million of goodwill as a result of the transaction. The Company also recorded $2.7 million of identifiable intangible assets consisting of customer contracts and backlog value which are being amortized on a straight-line basis over periods ranging from one year to three years.

All of the Company's acquisitions have been accounted for using the purchase method of accounting, and accordingly, the respective purchase prices were allocated to the assets (including intangible assets) acquired and liabilities assumed based on estimated fair values at the date of acquisition. The financial results from these acquisitions have been included in the Company's financial statements from the date of acquisition.

NET SALES

	Fiscal year ended			CHANGE	Change
(Dollars in millions)	2006	2005	2004	2006 VS. 2005	2005 vs. 2004
Communications	$156.2	138.0	137.8	13.2%	0.1%
Filtration/Fluid Flow	174.1	171.7	173.9	1.4%	(1.3)%
Test	128.6	119.4	110.4	7.7%	8.2%
Total	$458.9	429.1	422.1	6.9%	1.7%

COMMUNICATIONS

The $18.2 million or 13.2% increase in net sales in 2006 as compared to the prior year was due to: Hexagram and Nexus sales of $18.6 million and $9.6 million, respectively; partially offset by an $8.6 million decrease in sales of Comtrak's video security products; and $1.5 million of lower shipments of DCSI's AMR products.

The $1.5 million decrease in sales of DCSI's AMR products in 2006 as compared to 2005 was due to: an increase in sales to TXU of $19.9 million and other investor owned utilities (IOUs) of $3.0 million; offset by $16.2 million of lower AMR product sales to the electric utility cooperative (COOP) market due to the decrease in orders received during the second half of fiscal 2005; and an $8.1 million decrease in sales to Puerto Rico Electric Power Authority (PREPA) as the contract nears completion.

Comtrak's sales were $7.5 million, $16.1 million, and $5.6 million in 2006, 2005 and 2004, respectively. The decrease in sales in 2006 as compared to the prior year was due to an acceleration of shipments in 2005 to meet the customer's schedule. The increase in sales in 2005 versus 2004 was due to a delay in deliveries in 2004 as a result of a significant customer requesting Comtrak to modify its software operating system to provide enhanced "virus" protection within the product.

The $0.2 million or 0.1% increase in Communications net sales in 2005 as compared to the prior year was due to $10.5 million of higher shipments of SecurVision(R) products. This increase was almost entirely offset by a $10.3 million decrease in sales of AMR products. The decrease in sales of AMR products in 2005 versus 2004 was mainly due to the wind-down of a contract with PPL Electric Utilities Corporation (PPL). Sales to PPL decreased $19.3 million in 2005 to $2.4 million from $21.6 million in 2004. Sales to other IOUs, such as Bangor Hydro-Electric Company, Idaho Power Company, and PREPA decreased $17.9 million in 2005 versus 2004, and were partially offset by $7.2 million in sales to TXU and $19.8 million of additional sales to the COOP market and other customers.

FILTRATION/FLUID FLOW

Net sales in 2006 increased $2.4 million or 1.4% compared to 2005 primarily as a result of higher commercial aerospace shipments at PTI of $5.6 million, a net sales increase at Filtertek of $3.3 million driven by higher commercial shipments, partially offset by lower defense spares and T-700 shipments at VACCO of $6.6 million.

Net sales in 2005 decreased $2.2 million or 1.3% compared to 2004 primarily as a result of lower defense spares shipments at VACCO of $4.3 million, a net sales decrease at Filtertek of $0.5 million driven by lower automotive shipments, partially offset by higher commercial and military aerospace shipments at PTI of $2.6 million.

TEST

The net sales increase of $9.2 million or 7.7% in 2006 as compared to the prior year was mainly due to: a $10.2 million increase in net sales from the Company's U.S. operations driven by sales of additional test chambers and higher component sales, a $0.6 million increase in net sales from the Company's Asian operations; partially offset by a $1.6 million decrease in net sales from the Company's European operations due to the prior year completion of several test chamber projects.

The net sales increase of $9.0 million or 8.2% in 2005 as compared to 2004 was mainly due to: an $11.5 million increase in net sales from the Company's U.S. operations driven by the successful completion of the design on a large aircraft chamber project, additional test chamber installations, higher component sales, and the installation of several government shielding projects; a $4.3 million increase in sales from the Company's Asian operations; partially offset by a $6.9 million decrease in net sales from the Company's European operations due to the completion of two large test chamber projects in 2004.

ORDERS AND BACKLOG

New orders received in 2006 were $479.2 million, resulting in an order backlog of $253.4 million at September 30, 2006 as compared to an order backlog of $233.1 million at September 30, 2005. In 2006, the Company recorded $187.5 million of new orders related to Communications products (including $19.0 million of new orders and $6.0 million of acquired backlog from Hexagram and $16.7 million of new orders and $9.0 million of acquired backlog from Nexus), $172.1 million related to Filtration products, and $119.6 million related to Test products.

Within the Communications segment, DCSI received $129.3 million, $105.1 million and $106.3 million of new orders for its AMR products in 2006, 2005 and 2004, respectively. DCSI received $19.2 million of new orders from TXU in 2006. In addition, in November 2005, DCSI signed an agreement to provide equipment, software and services to PG&E with a potential contract value of up to approximately $310 million covering up to five million electric endpoints over a five-year deployment period beginning in 2007. DCSI received orders totaling $4.2 million from PG&E under this agreement during 2006. Also, in November 2005, Hexagram entered into a contract to provide equipment, software and services to PG&E in support of the gas utility portion of PG&E's AMI project. The total potential contract revenue from commencement through the five-year full deployment is up to approximately $225 million. Hexagram received orders totaling $0.7 million from PG&E under this agreement during 2006. See further discussion under "Pacific Gas & Electric."

In 2005, the Company recorded $117.2 million of new orders related to Communications products, $174.4 million related to Filtration products, and $121.5 million related to Test products.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses (SG&A) were $106.9 million, or 23.3% of net sales in 2006, $84.2 million, or 19.6% of net sales in 2005, and $77.3 million, or 18.3% of net sales in 2004.

The increase in SG&A expenses in 2006 as compared to the prior year was primarily due to: $7.5 million of SG&A expenses related to Nexus; $6.8 million of SG&A expenses related to Hexagram; $2.3 million of stock option expense and higher costs related to engineering and new product development.

The increase in SG&A expenses in 2005 as compared to 2004 was primarily due to an increase of $4.9 million associated with engineering, marketing and new product development within the Communications segment in pursuit of the IOU market.

AMORTIZATION OF INTANGIBLE ASSETS

Amortization of intangible assets was $6.9 million in 2006, $2.0 million in 2005 and $2.1 million in 2004. Amortization of intangible assets in 2006 included $2.7 million of amortization of acquired intangible assets related to the Hexagram and Nexus acquisitions, as described in Note 2 to the Consolidated Financial Statements. The amortization of acquired intangible assets related to Hexagram and Nexus are included in the Corporate operating segment's results. The remaining amortization expenses consist of other identifiable intangible assets (primarily software, patents and licenses). In March 2006, the Company began amortizing DCSI's TNG software and during 2006, the Company recorded $2.2 million of amortization related to its TNG software.

OTHER (INCOME) AND EXPENSES, NET

Other (income) and expenses, net, were $(2.8) million, $(1.6) million and $0.6 million in 2006, 2005 and 2004, respectively. Other (income) and expenses, net, in 2006 consisted primarily of the following items: $(1.8) million non-cash gain representing the reversal of a liability related to an indemnification obligation with respect to a previously divested subsidiary; $(2.3) million of royalty income; partially offset by a $0.2 million charge related to the termination of a subcontract manufacturer.

Other (income) and expenses, net, in 2005 consisted primarily of: $(2.2) million of royalty income; and a $0.5 million charge related to the termination of a supply agreement with a medical device customer.

Other (income) and expenses, net, in 2004 consisted primarily of: $0.8 million of exit costs related to the Puerto Rico facility; a $(0.6) million gain from the settlement of a claim related to a former defense subsidiary divested in 1999; and a $0.4 million charge for the settlement of a claim involving a former defense subsidiary divested in 1996.

ASSET IMPAIRMENT -- 2005

In June 2005, the Company abandoned its plans to commercialize certain sensor products within the Filtration/Fluid Flow segment. This action resulted in an asset impairment charge of $0.8 million to write off certain patents and a related licensing agreement to their respective fair market values. The Company ended its development efforts on this program after it determined that the market was not developing as quickly as anticipated and the expected costs and time frame to fully commercialize the products were not acceptable.

EARNINGS BEFORE INTEREST AND TAXES (EBIT)

The Company evaluates the performance of its operating segments based on EBIT, which the Company defines as earnings from continuing operations before interest and taxes.

EBIT is not a defined GAAP measure. However, the Company believes that EBIT provides investors and Management with a valuable and alternative method for assessing the Company's operating results. Management evaluates the performance of its operating segments based on EBIT and believes that EBIT is useful to investors to demonstrate the operational profitability of the Company's business segments by excluding interest and taxes, which are generally accounted for across the entire company on a consolidated basis. EBIT is also one of the measures Management uses to determine resource allocations and incentive compensation.

	Fiscal year ended			CHANGE 2006	Change 2005
(Dollars in millions)	2006	2005	2004	VS. 2005	vs. 2004
Communications	$ 28.3	38.8	38.4	(27.1)%	1.0%
% of net sales	18.1%	28.1%	27.9%	(10.0)%	0.2%
Filtration/Fluid Flow	19.5	22.4	21.8	(12.9)%	2.8%
% of net sales	11.2%	13.1%	12.5%	(1.9)%	0.6%
Test	15.0	12.2	11.3	23.0%	8.0%
% of net sales	11.7%	10.2%	10.2%	1.5%	--%
Corporate	(15.2)	(11.4)	(11.8)	33.3%	(3.4)%
Total	$ 47.6	62.0	59.7	(23.2)%	3.9%
% of net sales	10.4%	14.4%	14.1%	(4.0)%	0.3%

The reconciliation of EBIT to a GAAP financial measure is as follows:

(dollars in millions)	2006	2005	2004
EBIT	$ 47.6	62.0	59.7
Add: Interest income	1.3	1.9	0.8
Less: Income taxes	(17.6)	(20.4)	(22.7)
Net earnings from continuing operations	$ 31.3	43.5	37.8

COMMUNICATIONS

The decrease in EBIT in 2006 as compared to 2005 was due to: a $7.8 million decrease at DCSI due to changes in product mix (IOU vs. COOP), charges related to a terminated subcontract manufacturer, warranty costs and amortization of TNG software; a $3.8 million decrease at Comtrak due to lower shipments; a $0.7 million loss at Nexus due to the timing of customer deployments and additional SG&A spending related to engineering and new product initiatives; partially offset by a $1.8 million contribution from Hexagram.

The increase in EBIT in 2005 as compared to the prior year was due to: a $4.6 million increase at Comtrak due to significantly higher shipments; partially offset by a $4.2 million decrease at DCSI, which continued to increase its engineering and new product development expenditures in order to accommodate the growth in the AMR/AMI markets, and to further differentiate its technology from the competition.

FILTRATION/FLUID FLOW

EBIT decreased in 2006 as compared to 2005 primarily due to: a $4.3 million decrease at VACCO due to significantly lower defense spares shipments; a $1.4 million decrease at Filtertek partially due to increasing raw material costs on petroleum based resins; partially offset by a $2.8 million increase at PTI due to higher shipments of aerospace products. The 2005 operating results for Filtertek included a $1.9 million gain related to the termination of a supply agreement with a medical device customer that was not repeated in 2006.

EBIT increased in 2005 as compared to the prior year primarily due to: a $2.5 million increase at Filtertek, which included a $1.9 million gain related to the termination of a supply agreement with a medical device customer; a $1.4 million increase at PTI due to higher shipments of aerospace products; partially offset by the $0.8 million asset impairment charge at PTI; and a $3.3 million decrease at VACCO due to significantly lower defense spares shipments. In 2005, Filtertek experienced an increase in its raw material costs on petroleum based resins which negatively impacted EBIT.

TEST

The increase in EBIT in 2006 as compared to the prior year was mainly due to: a $2.1 million increase in EBIT from the Company's U.S. operations driven by sales of additional test chambers and higher component sales, a $0.4 million increase in EBIT from the Company's European operations, and a $0.3 million increase in EBIT from the Company's Asian operations.

EBIT in 2005 included: a $0.9 million increase in EBIT from the Company's U.S. operations driven by favorable changes in sales mix resulting from additional sales of antennas and other components partially offset by installation cost overruns incurred on certain government shielding projects, as well as increased material costs for steel and copper.

CORPORATE

Corporate office operating charges included in consolidated EBIT increased by $3.8 million in 2006 as compared to 2005 mainly due to: $2.7 million of pre-tax amortization of acquired intangible assets related to Nexus and Hexagram; $2.3 million of pre-tax stock option expense; partially offset by a $1.8 million non-cash gain representing the reversal of a liability related to an indemnification obligation with respect to a previously divested subsidiary. Corporate office operating charges included in consolidated EBIT decreased by $0.4 million in 2005 as compared to 2004. Fiscal 2005 included an increase of $0.5 million for professional fees and 2004 included $0.9 million of severance related costs not repeated in 2005. The "Reconciliation to Consolidated Totals (Corporate)" in note 15 to the consolidated financial statements represents Corporate office operating charges.

INTEREST INCOME

Interest income was $1.3 million in 2006, $1.9 million in 2005 and $0.8 million in 2004. The decrease in interest income in 2006 as compared to 2005 was due to lower average cash balances on hand resulting from the 2006 acquisitions. The increase in interest income in 2005 as compared to the prior year was due to higher average cash balances on hand during the year and a $0.2 million refund of look back interest related to income taxes.

INCOME TAX EXPENSE

The effective tax rate for continuing operations in 2006 was 36.0% compared to 31.9% in 2005 and 37.6% in 2004. The increase in the effective tax rate in 2006 as compared to the prior year was due to: the effect of the foreign earnings repatriation increased 2006 income tax expense by $2.4 million and the effective rate by 4.8%; the adoption of SFAS 123(R) increased tax expense by $0.7 million and the effective rate by 1.4%; the lower volume of profit contributions of the Company's foreign operations (primarily Puerto Rico due to the lower sales to PREPA) adversely impacted the tax rate; partially offset by the effect of a favorable change in tax contingencies not related to the research tax credit which decreased tax expense by $1.4 million and the effective tax rate by 2.9% and the net effect of the research tax credit which favorably impacted tax expense by $2.5 million and the effective tax rate by 5%. The decrease in the effective tax rate for continuing operations in 2005 as compared to 2004 was due to the timing and volume of profit contributions of DCSI's foreign operations (Puerto Rico), which resulted in a 4.6% favorable adjustment to the Company's foreign tax rate differential.

During 2006, the Company determined that state tax expense had not been accurately recorded in the financial statements for years 2001 through 2005. The effect in any individual prior year was not material to the Company's results of operations, financial position or cash flows. The Company adopted the provisions of SEC Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" and recorded $2.4 million as a cumulative credit adjustment to 2006 beginning retained earnings.

CAPITAL RESOURCES AND LIQUIDITY

Working capital (current assets less current liabilities) decreased to $131.4 million at September 30, 2006 from $197.2 million at September 30, 2005. During 2006, cash and cash equivalents decreased $67.7 million, primarily due to the $92 million spent on acquisitions.

The $15.0 million increase in accounts receivable at September 30, 2006 is mainly due to: $8.3 million related to Nexus and Hexagram; and $5.7 million related to the Filtration segment due to timing and volume of sales. The $2.3 million increase in inventories at September 30, 2006 is mainly due to a $4.4 million increase related to Hexagram, partially offset by a $3.8 million decrease at DCSI. Accounts payable increased by $10.2 million at September 30, 2006, of which $3.0 million related to Nexus and Hexagram and $4.6 million related to the timing of vendor payments at DCSI.

Net cash provided by operating activities was $58.6 million, $68.6 million and $61.0 million in 2006, 2005 and 2004, respectively. The decrease in 2006 is related to lower net earnings in the current year. The increase in 2005 as compared to 2004 is the result of higher earnings and lower cash requirements related to MicroSep.

Capital expenditures for continuing operations were $9.1 million, $8.8 million and $10.8 million in 2006, 2005 and 2004, respectively. Major expenditures included manufacturing equipment and facility modifications used in the Filtration segment. There were no commitments outstanding that were considered material for capital expenditures at September 30, 2006.

At September 30, 2006, intangible assets, net, of $59.2 million included $45.2 million of capitalized software. Approximately $40.0 million of the capitalized software balance represents external development costs on software development called "TNG" within the Communications segment to further penetrate the IOU market. TNG is being deployed to efficiently handle the additional levels of communications dictated by the size of the service territories and the frequency of reads that are required under time-of-use or critical peak pricing scenarios to meet the requirements of large IOUs. At September 30, 2006, the Company had approximately $5 million of commitments related to TNG version 1.6.3 which is expected to be spent over the next six months. The Company expects to spend up to approximately $10 million in fiscal 2007 on TNG. Amortization of TNG is on a straight-line basis over seven years and began in March 2006. The Company recorded $2.2 million in amortization expense related to TNG during 2006.

At September 30, 2006, the Company had an available net operating loss (NOL) carryforward for U.S. federal tax purposes of approximately $15 million. This NOL will expire between 2019 and 2025, and will be available to reduce future Federal income tax cash payments.

The closure and relocation of the Filtertek Puerto Rico facility was completed in March 2004. The Puerto Rico facility is included in other current assets with a carrying value of $3.6 million at

September 30, 2006. The facility is being marketed for sale.

During 2005, the Company reached a settlement in the defense of a certain revenue-generating patent used in the Filtration business. Under the terms of the agreement, the Company received a cash payment of $1.5 million, and in 2005 the Company recognized a gain of $0.3 million, after deducting $0.2 million of professional fees related to the settlement. The unrecognized gain is being recorded on a straight-line basis in Other (income) and expenses, net, over the remaining patent life, through 2011.

In 2004, the Company received $2.1 million as final payment on the note receivable from the sale of the Riverhead, NY, property which was sold in 1999.

PACIFIC GAS & ELECTRIC

In November 2005, DCSI entered into a contract to provide equipment, software and services to Pacific Gas & Electric (PG&E) in support of the electric portion of PG&E's Advanced Metering Infrastructure (AMI) project. PG&E's current AMI project plan calls for the purchase of TWACS communication equipment for up to approximately five million electric customers over a five-year period after the commencement of full deployment. The total anticipated contract value from commencement through the five-year full deployment period is expected to be up to approximately $310 million. PG&E also has the right to purchase additional equipment and services to support existing and new customers through the 20-year term of the contract. Equipment will be purchased by PG&E only upon issuance of purchase orders and release authorizations. PG&E will continue to have the right to purchase products or services from other suppliers for the electric portion of the AMI project. On July 20, 2006, the California Public Utilities Commission approved PG&E's AMI project. DCSI has agreed to deliver to PG&E versions of its newly developed TNG software as they become available and are tested. Delivery of the final version for which DCSI has committed is currently anticipated in the fourth quarter of fiscal 2007. In accordance with U.S. generally accepted accounting standards, the Company will defer all revenue related to the DCSI arrangement until all software is delivered and acceptance criteria have been met. The contract provides for liquidated damages in the event of DCSI's late development or delivery of hardware and software, and includes indemnification and other customary provisions. The contract may be terminated by PG&E for default, for its convenience and in the event of a force majeure lasting beyond certain prescribed periods. The Company has guaranteed the obligations of DCSI under the contract. If PG&E terminates the contract for its convenience, DCSI will be entitled to recover certain costs.

In November 2005, Hexagram entered into a contract to provide equipment, software and services to PG&E in support of the gas utility portion of PG&E's AMI project. The total anticipated contract revenue from commencement through the five-year full deployment is expected to be approximately $225 million. As with DCSI's contract with PG&E, equipment will be purchased only upon issuance of purchase orders and release authorizations, and PG&E will continue to have the right to purchase products or services from other suppliers for the gas utility portion of the AMI project. On July 20, 2006, the California Public Utilities Commission approved PG&E's AMI project. The contract provides for liquidated damages in the event of late deliveries, includes indemnification and other customary provisions, and may be terminated by PG&E for default, for its convenience and in the event of a force majeure lasting beyond certain prescribed periods. The Company has guaranteed the performance of the contract by Hexagram.

DIVESTITURES

Effective April 2, 2004, the Company completed the sale of PTI Advanced Filtration Inc. (Oxnard, California) and PTI Technologies Limited (Sheffield, England) to domnick hunter group plc for $18.0 million in cash. On June 8, 2004, the Company completed the sale of PTI S.p.A. (Milan, Italy) to a group of investors comprised of the subsidiary's senior management for $5.3 million. An after-tax gain of $1.6 million related to the sale of these MicroSep businesses is reflected in the Company's 2004 results in discontinued operations. These businesses are accounted for as a discontinued operation in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," and accordingly, amounts in the financial statements and related notes for 2004, reflect discontinued operations presentation.

BANK CREDIT FACILITY

Effective October 6, 2004, the Company entered into a $100 million five-year revolving bank credit facility with a $50 million increase option that has a final maturity and expiration date of October 6, 2009. The credit facility is available for direct borrowings and/or the issuance of letters of credit, and is provided by a group of six banks, led by Wells Fargo Bank as agent.

The credit facility requires, as determined by certain financial ratios, a commitment fee ranging from 17.5 to 27.5 basis points per annum on the unused portion. The terms of the facility provide that interest on borrowings may be calculated at a spread over the LIBOR or based on the prime rate, at the Company's election. The credit facility is secured by the unlimited guaranty of the Company's material domestic subsidiaries and a 65% pledge of the material foreign subsidiaries' share equity. The financial covenants of the credit facility include limitations on leverage, minimum consolidated EBITDA and minimum net worth.

At September 30, 2006, the Company had approximately $99.2 million available to borrow under the credit facility in addition to its $36.8 million cash on hand. At September 30, 2006, the Company had no borrowings, and outstanding letters of credit of $1.5 million ($0.8 million outstanding under the credit facility). As of September 30, 2006, the Company was in compliance with all bank covenants.

Cash flow from operations and borrowings under the bank credit facility are expected to provide adequate resources to meet the Company's capital requirements and operational needs for the foreseeable future.

CONTRACTUAL OBLIGATIONS

The following table shows the Company's contractual obligations as of September 30, 2006:

(dollars in millions) Payments due by period

Contractual Obligations	Total	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years
Long-Term Debt Obligation	$ --	--	--	--	--
Capital Lease Obligations	0.9	0.4	0.3	0.2	--
Operating Lease Obligations	22.3	7.1	7.9	4.0	3.3
Purchase Obligations(1)	5.0	5.0	--	--	--
Total	$28.2	12.5	8.2	4.2	3.3

(1) A purchase obligation is defined as a legally binding and enforceable agreement to purchase goods and services that specifies all significant terms. Since the majority of the Company's purchase orders can be cancelled, they are not included in the table above. TNG software development costs through version 1.6.3 are included.

The Company has no off balance sheet arrangements outstanding at September 30, 2006.

SHARE REPURCHASES

In August 2006, the Company's Board of Directors authorized an open market common stock repurchase program for up to 1.2 million shares, subject to market conditions and other factors which covers the period through September 30, 2008. There were no stock repurchases during fiscal 2006. The Company repurchased 670,072 and 312,400 shares in 2005 and 2004, respectively, under a previously authorized program.

PENSION FUNDING REQUIREMENTS

The minimum cash funding requirements related to the Company's defined benefit pension plans are zero in 2007, approximately $1 million in 2008 and approximately $1 million in 2009. The Company made a voluntary cash contribution of $1.4 million in 2006.

OTHER

Management believes that, for the periods presented, inflation has not had a material effect on the Company's results of operations.

The Company is currently involved in various stages of investigation and remediation relating to environmental matters. Based on current information available, Management does not believe the aggregate costs involved in the resolution of these matters will have a material adverse effect on the Company's operating results, capital expenditures or competitive position.

MARKET RISK ANALYSIS

MARKET RISK EXPOSURE

Market risks relating to the Company's operations result primarily from changes in interest rates and changes in foreign currency exchange rates.

At September 30, 2006 and 2005, the Company had no obligations related to interest rate swaps. During 2004, in conjunction with the sale of PTI S.p.A., the Company repaid its $8.0 million Euro-denominated debt, and at the same time, the Company terminated its $5.0 million interest rate swap obligation, resulting in a cash payment of $0.1 million by the Company.

The Company is also subject to foreign currency exchange rate risk inherent in its sales commitments, anticipated sales, anticipated purchases and assets and liabilities denominated in currencies other than the U.S. dollar. The foreign currency most significant to the Company's operations is the Euro. Net sales to customers outside of the United States were $103.0 million, $103.8 million, and $91.5 million in 2006, 2005 and 2004, respectively. The Company hedges certain foreign currency commitments by purchasing foreign currency forward contracts. The estimated fair value of open forward contracts at September 30, 2006 was not material.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with GAAP requires Management to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying consolidated financial statements. In preparing these financial statements, Management has made its best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. The Company does not believe there is a great likelihood that materially different amounts would be reported under different conditions or using different assumptions related to the accounting policies described below. However, application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. The Company's senior Management discusses the critical accounting policies described below with the Audit and Finance Committee of the Company's Board of Directors on a periodic basis.

The following discussion of critical accounting policies is intended to bring to the attention of readers those accounting policies which Management believes are critical to the Consolidated Financial Statements and other financial disclosure. It is not intended to be a comprehensive list of all significant accounting policies that are more fully described in Note 1 of Notes to Consolidated Financial Statements.

REVENUE RECOGNITION

COMMUNICATIONS UNIT: Within the Communications unit, approximately 95% of the unit's revenue arrangements (approximately 30% of consolidated revenues) contain software components. Revenue under these arrangements is recognized in accordance with Statement of Position 97-2 (SOP 97-2), "Software Revenue Recognition," as amended by SOP 98-9, "Modification of SOP 97-2, Software Revenue Recognition, with Respect to Certain Transactions." The application of software revenue recognition requires judgment, including the determination of whether a software arrangement includes multiple elements and estimates of the fair value of the elements, or vendor-specific objective evidence of fair value ("VSOE"). Changes to the elements in a software arrangement, and the ability to identify VSOE for those elements could materially impact the amount of earned and/or deferred revenue. There have been no material changes to these estimates for the financial statement periods presented and the Company believes that these estimates generally should not be subject to significant variation in the future. The remaining 5% of the unit's revenues represent products sold under a single element arrangement and are recognized when products are delivered to unaffiliated customers.

FILTRATION/FLUID FLOW UNIT: Within the Filtration/Fluid Flow operating unit, approximately 75% of operating unit revenues (approximately 30% of consolidated revenues) are recognized when products are delivered (when title and risk of ownership transfers) or when services are performed for unaffiliated customers.

Approximately 25% of operating unit revenues (approximately 10% of consolidated revenues) are recorded under the percentage-of-completion provisions of SOP 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" because the Company manufactures complex products for aerospace and military customers under production contracts. The percentage-of-completion method of accounting involves the use of various estimating techniques to project costs at completion. These estimates involve various assumptions and projections relative to the outcome of future events over a period of several years, including future labor productivity and availability, the nature and complexity of the work to be performed, availability of materials, the impact of delayed performance, and the timing of product deliveries. These estimates are based on Management's judgment and the Company's substantial experience in developing these types of estimates. Changes in underlying assumptions/estimates may adversely affect financial performance if they increase estimated project costs at completion, or positively affect financial performance if they decrease estimated project costs at completion. Due to the nature of these contracts and the operating unit's cost estimating process, the Company believes that these estimates generally should not be subject to significant variation in the future. There have been no material changes to these estimates for the financial statement periods presented. The Company regularly reviews its estimates to assess revisions in contract values and estimated costs at completion.

TEST UNIT: Within the Test unit, approximately 60% of revenues (approximately 20% of consolidated revenues) are recognized when products are delivered (when title and risk of ownership transfers) or when services are performed for unaffiliated customers. Certain arrangements contain multiple elements which are accounted for under the provisions of EITF 00-21, "Revenue Arrangements with Multiple Deliverables." The application of EITF 00-21 requires judgment as to whether the deliverables can be divided into more than one unit of accounting and whether the separate units of accounting have value to the customer on a stand-alone basis. Changes to these elements could affect the timing of revenue recognition. There have been no material changes to these elements for the financial statement periods presented.

Approximately 40% of the unit's revenues (approximately 10% of consolidated revenues) are recorded under the percentage-of-completion provisions of SOP 81-1, "Accounting for the Performance of Construction-Type and Certain Production-Type Contracts" due to the complex nature of the enclosures that are designed and produced under these contracts. As discussed above, this method of accounting involves the use of various estimating techniques to project costs at completion, which are based on Management's judgment and the Company's substantial experience in developing these types of estimates. Changes in underlying assumptions/estimates may adversely or positively affect financial performance. Due to the nature of these contracts and the operating unit's cost estimating process, the Company believes that these estimates generally should not be subject to significant variation in the future. There have been no material changes to these estimates for the financial statement periods presented. The Company regularly reviews its contract estimates to assess revisions in contract values and estimated costs at completion.

INVENTORY

Inventories are valued at the lower of cost (first-in, first-out) or market value. Management regularly reviews inventories on hand compared to historical usage and estimated future usage and sales. Inventories under long-term contracts reflect accumulated production costs, factory overhead, initial tooling and other related costs less the portion of such costs charged to cost of sales and any unliquidated progress payments. In accordance with industry practice, costs incurred on contracts in progress include amounts relating to programs having production cycles longer than one year, and a portion thereof may not be realized within one year.

INCOME TAXES

The Company operates in numerous taxing jurisdictions and is subject to examination by various U.S. Federal, state and foreign jurisdictions for various tax periods. Additionally, the Company has retained tax liabilities and the rights to tax refunds in connection with various divestitures of businesses in prior years. The Company's income tax positions are based on research and interpretations of the income tax laws and rulings in each of the jurisdictions in which the Company does business. Due to the subjectivity of interpretations of laws and rulings in each jurisdiction, the differences and interplay in tax laws between those jurisdictions, as well as the inherent uncertainty in estimating the final resolution of complex tax audit matters, Management's estimates of income tax liabilities may differ from actual payments or assessments.

While the Company has support for the positions taken on its tax returns, taxing authorities are increasingly asserting alternate interpretations of laws and facts, and are challenging cross jurisdictional transactions. Cross jurisdictional transactions between the Company's subsidiaries involving transfer prices for products and services, as well as various U.S. federal, state and foreign tax matters, comprise the Company's income tax exposures. Management regularly assesses the Company's position with regard to tax exposures and records liabilities for these uncertain tax positions and related interest and penalties, if any, according to the principles of SFAS No. 5, "Accounting for Contingencies." The Company has recorded an accrual that reflects Management's estimate of the likely outcome of current and future audits. A final determination of these tax audits or changes in Management's estimates may result in additional future income tax expense or benefit.

At the end of each interim reporting period, Management estimates the effective tax rate expected to apply to the full fiscal year. The estimated effective tax rate contemplates the expected jurisdiction where income is earned, as well as tax planning strategies. Current and projected growth in income in higher tax jurisdictions may result in an increasing effective tax rate over time. If the actual results differ from Management's estimates, Management may have to adjust the effective tax rate in the interim period such determination is made.

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets may be reduced by a valuation allowance if it is more likely than not that some portion of all of the deferred tax assets will not be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company regularly reviews its deferred tax assets for recoverability and establishes a valuation allowance when Management believes it is more likely than not such assets will not be recovered, taking into consideration historical operating results, expectations of future earnings, tax planning strategies, and the expected timing of the reversals of existing temporary differences.

GOODWILL AND OTHER LONG-LIVED ASSETS

In accordance with SFAS 142, Management annually reviews goodwill and other long-lived assets with indefinite useful lives for impairment or whenever events or changes in circumstances indicate the carrying amount may not be recoverable. If the Company determines that the carrying value of the long-lived asset may not be recoverable, a permanent impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value. Fair value is measured based on a discounted cash flow method using a discount rate determined by Management to be commensurate with the risk inherent in the Company's current business model. The estimates of cash flows and discount rate are subject to change due to the economic environment, including such factors as interest rates, expected market returns and volatility of markets served. Management believes that the estimates of future cash flows and fair value are reasonable; however, changes in estimates could result in impairment charges. SFAS 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS 144.

PENSION PLANS AND OTHER POSTRETIREMENT BENEFIT PLANS

The measurement of liabilities related to pension plans and other post-retirement benefit plans is based on Management's assumptions related to future events including interest rates, return on pension plan assets, rate of compensation increases, and health care cost trend rates. Actual pension plan asset performance will either decrease or increase unamortized pension losses that will affect net earnings in future years. Depending upon the performance of the equity and bond markets in 2007, the Company could be required to record a charge to equity. In addition, if the discount rate was decreased by 25 basis points from 5.75% to 5.50%, the accumulated benefit obligation for the defined benefit plan would increase by approximately $1.6 million and result in an additional after-tax charge to shareholders' equity of approximately $1.0 million. The discount rate used in measuring the Company's pension and postretirement welfare obligations was developed by matching yields of actual high-quality corporate bonds to expected future pension plan cash flows (benefit payments). Over 500 Aa-rated, non-callable bonds with a wide range of maturities were used in the analysis. After using the bond yields to determine the present value of the plan cash flows, a single representative rate that resulted in the same present value was developed.

OTHER MATTERS

CONTINGENCIES

As a normal incident of the businesses in which the Company is engaged, various claims, charges and litigation are asserted or commenced against the Company. Lindgren is involved in a contract dispute with a prime contractor involving the assertion of certain construction delay damages of approximately $3.7 million. The project was completed in 2005. Lindgren vigorously denies responsibility for this delay and for these damages, and has asserted a claim against the prime contractor of $0.9 million based on damages suffered by Lindgren. Lindgren continues to aggressively defend its position and pursue its right to affirmative damages however, there can be no assurance of the outcome at this time. In the opinion of Management, final judgments, if any, which might be rendered against the Company are adequately reserved, covered by insurance, or are not likely to have a material adverse effect on its financial statements.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risks relating to the Company's operations result primarily from changes in interest rates and changes in foreign currency exchange rates. At September 30, 2006 and 2005, the Company had no obligations related to interest rate swaps. During 2004, in conjunction with the sale of PTI S.p.A., the Company repaid its $8.0 million Euro-denominated debt and at the same time, the Company terminated its $5.0 million interest rate swap obligation resulting in a cash payment of $0.1 million by the Company. See further discussion in "Management's Discussion and Analysis -- Market Risk Analysis" regarding the Company's market risks.

CONTROLS AND PROCEDURES

The Company carried out an evaluation under the supervision of and with the participation of Management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective excluding the Hexagram and Nexus acquisitions. Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in company reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within time periods specified in the Securities and Exchange Commission's rules and forms. There have been no significant changes in the Company's internal controls or in other factors during the period covered by this report that have materially affected, or are reasonably likely to materially affect those controls and procedures.

NEW ACCOUNTING PRONOUNCEMENTS

In December 2004, the FASB issued SFAS No. 123(R), "Share-Based Payment" (SFAS 123(R)). This Statement replaces SFAS No. 123, "Accounting for Stock-Based Compensation" and supersedes APB No. 25, "Accounting for Stock Issued to Employees." SFAS 123(R) requires all stock-based compensation to be recognized as an expense in the financial statements and that such cost be measured according to the fair value of stock options. The Company adopted the provisions of this Statement in the first quarter of fiscal 2006 on a prospective basis.

In December 2004, the FASB issued FASB Staff Position FAS 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004 (FSP 109-2)." The American Jobs Creation Act of 2004, (the "Act") provides for a special one-time deduction of 85 percent of certain foreign earnings repatriated into the U.S. from non-U.S. subsidiaries through September 30, 2006. During fiscal 2006, the Company repatriated $39.5 million of foreign earnings which qualify for the special one-time deduction. Tax expense of $2.4 million was recorded in fiscal 2006 as a result of this repatriation.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109." This Interpretation is effective for ESCO beginning October 1, 2007. This Interpretation prescribes a recognition threshold and measurement process for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company is currently evaluating the adoption of this Interpretation and does not currently have an estimate of the impact on the consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158, "Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158), which amends SFAS 87 and SFAS 106 to require recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. Under SFAS 158, gains and losses, prior service costs and credits, and any remaining transition amounts under SFAS 87 and SFAS 106 that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects. The measurement date -- the date at which the benefit obligation and plan assets are measured -- is required to be the Company's fiscal year-end, which is the date the Company currently uses. SFAS 158 is effective for publicly held companies for fiscal years ending after December 15, 2006. The adoption of SFAS 158 is not expected to have a material impact to the Company's financial position or results of operations.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB No. 108), which addresses the diversity in practice in quantifying financial statement misstatements and provides interpretative guidance regarding the consideration given to prior year misstatements when determining materiality in current year financial statements. During 2006, the Company adopted the provisions of SAB No. 108 and recorded $2.4 million as a cumulative credit adjustment to 2006 beginning retained earnings.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" (SFAS 157), which defines fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS 157 is not expected to have a material impact to the Company's financial position or results of operations.

FORWARD-LOOKING INFORMATION

Statements regarding future events and the Company's future results that are based on current expectations, estimates, forecasts and projections about the Company's performance and the industries in which the Company operates, the Company's ability to utilize NOLs, adequacy of the Company's credit facility and future cash flows, estimates of anticipated contract costs and revenues, the timing, amount and success of claims for research credits, the success of software development efforts and resulting costs, acceptance by PG&E of the final version of DCSI's TNG software, growth in the AMR market, potential customer contracts, the anticipated value of the PG&E contract, the outcome of current litigation, claims and charges, recoverability of deferred tax assets, continued reinvestment of foreign earnings, the impact of SFAS 158, future costs relating to environmental matters, share repurchases, investments, sustained performance improvement, performance improvement initiatives, growth opportunities, new product development, the Company's ability to increase shareholder value, acquisitions, and the beliefs and assumptions of Management contained in the Letter to Our Shareholders (pages 1-2), the Report of the Chief Financial Officer (page 12), and Management's Discussion and Analysis and other statements contained herein which are not strictly historical are considered "forward-looking statements" within the meaning of the safe harbor provisions of the federal securities laws. Words such as expects, anticipates, targets, goals, projects, intends, plans, believes, estimates, variations of such words, and similar expressions are intended to identify such forward-looking statements. Investors are cautioned that such statements are only predictions, speak only as of the date of this report, and the Company undertakes no duty to update. The Company's actual results in the future may differ materially from those projected in the forward-looking statements due to risks and uncertainties that exist in the Company's operations and business environment including, but not limited to: actions by the California Public Utility Commission; PG&E's Board of Directors or PG&E's management impacting PG&E's AMI projects; the timing and success of DCSI's software development efforts; the timing and content of purchase order releases under the PG&E contracts; and DCSI's and Hexagram's successful performance of the PG&E contracts; the timing and execution of real estate sales; termination for convenience of customer contracts; timing and magnitude of future contract awards; weakening of economic conditions in served markets; the success of the Company's competitors; changes in customer demands or customer insolvencies; competition; intellectual property rights; technical difficulties; the availability of selected acquisitions; the timing, pricing and availability of shares offered for sale; delivery delays or defaults by customers; performance issues with key customers, suppliers and subcontractors; material changes in the costs of certain raw materials; the successful sale of the Company's Puerto Rico facility; collective bargaining and labor disputes; changes in laws and regulations including but not limited to changes in accounting standards and taxation requirements; costs relating to environmental matters; litigation uncertainty; and the Company's successful execution of internal operating plans.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands, except per share amounts) Years ended September 30,	2006	2005	2004
Net sales	$458,865	429,115	422,085
Costs and expenses:			
Cost of sales	300,309	281,654	282,369
Selling, general and administrative expenses	106,882	84,241	77,296
Amortization of intangible assets	6,872	1,973	2,122
Interest income, net	(1,286)	(1,900)	(844)
Other (income) and expenses, net	(2,814)	(1,550)	578
Asset impairment	--	790	--
Total costs and expenses	409,963	365,208	361,521
Earnings before income tax	48,902	63,907	60,564
Income tax expense	17,622	20,363	22,748
Net earnings from continuing operations	31,280	43,544	37,816
Loss from discontinued operations, net of tax benefit: 2004, $(1,295)	--	--	(3,737)
Gain on sale of discontinued operations, net of tax benefit: 2004, $(1,186)	--	--	1,592
Net loss from discontinued operations	--	--	(2,145)
Net earnings	$ 31,280	43,544	35,671
Earnings per share:			
Basic:			
Continuing operations	$ 1.22	1.71	1.47
Discontinued operations	--	--	(0.09)
Net earnings	$ 1.22	1.71	1.38
Diluted:			
Continuing operations	$ 1.19	1.66	1.42
Discontinued operations	--	--	(0.08)
Net earnings	$ 1.19	1.66	1.34
Average common shares outstanding (in thousands):			
Basic	25,718	25,511	25,803
Diluted	26,386	26,306	26,648

See accompanying notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

Years ended September 30,	2006	2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 36,819	104,484
Accounts receivable, less allowance for doubtful accounts of $798 and $585 in 2006 and 2005, respectively	83,816	68,819
Costs and estimated earnings on long-term contracts, less progress billings of $4,405 and $7,033 in 2006 and 2005, respectively	1,345	4,392
Inventories	50,984	48,645
Current portion of deferred tax assets	24,251	25,271
Other current assets	10,042	8,394
Total current assets	207,257	260,005
PROPERTY, PLANT AND EQUIPMENT:		
Land and land improvements	5,497	5,493
Buildings and leasehold improvements	46,089	42,918
Machinery and equipment	86,312	76,741
Construction in progress	1,444	1,108
	139,342	126,260
Less accumulated depreciation and amortization	70,588	59,070
Net property, plant and equipment	68,754	67,190
Goodwill	143,450	68,880
Intangible assets, net	59,202	21,545
Other assets	10,031	6,152
	$488,694	423,772

See accompanying notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

Years ended September 30,	2006	2005
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Short-term borrowings and current maturities of long-term debt	$ --	--
Accounts payable	39,496	29,299
Advance payments on long-term contracts, less costs incurred of $19,532 and $10,949 in 2006 and 2005, respectively	7,367	6,773
Accrued salaries	13,932	12,024
Accrued other expenses	15,100	14,661
Total current liabilities	75,895	62,757
Deferred revenue	7,458	3,134
Pension obligations	13,143	17,481
Other liabilities	15,764	9,376
Long-term debt	--	--
Total liabilities	112,260	92,748
SHAREHOLDERS' EQUITY:		
Preferred stock, par value $.01 per share, authorized 10,000,000 shares	--	--
Common stock, par value $.01 per share, authorized 50,000,000 shares; Issued 29,030,995 and 28,738,958 shares in 2006 and 2005, respectively	290	287
Additional paid-in capital	236,390	228,317
Retained earnings	193,046	159,363
Accumulated other comprehensive loss	(2,070)	(5,566)
	427,656	382,401
Less treasury stock, at cost (3,166,026 and 3,175,626 common shares in 2006 and 2005, respectively)	(51,222)	(51,377)
Total shareholders' equity	376,434	331,024
	$488,694	423,772

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In thousands) Years ended September 30,	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance, September 30, 2003	13,933	$139	216,506	80,292	(4,982)	(16,566)	275,389
Comprehensive income:							
Net earnings	--	--	--	35,671	--	--	35,671
Translation adjustments	--	--	--	--	2,703	--	2,703
Minimum pension liability, net of tax of $815	--	--	--	--	(1,514)	--	(1,514)
Interest rate swap adjustment net of tax benefit of $(51)	--	--	--	--	95	--	95
Comprehensive income							36,955
Stock options and stock compensation plans, net of tax benefit of $(1,939)	216	3	5,205	--	--	45	5,253
Purchases into treasury	--	--	--	--	--	(9,981)	(9,981)
Balance, September 30, 2004	14,149	142	221,711	115,963	(3,698)	(26,502)	307,616
Comprehensive income:							
Net earnings	--	--	--	43,544	--	--	43,544
Translation adjustments	--	--	--	--	680	--	680
Minimum pension liability, net of tax of $1,372	--	--	--	--	(2,548)	--	(2,548)
Comprehensive income							41,676
Stock options and stock compensation plans, net of tax benefit of $(3,032)	222	1	6,606	--	--	53	6,660
Purchases into treasury	--	--	--	--	--	(24,928)	(24,928)
100 percent stock dividend	14,368	144	--	(144)	--	--	--
Balance, September 30, 2005	28,739	287	228,317	159,363	(5,566)	(51,377)	331,024
SAB 108 Cumulative effect adjustment	--	--	--	2,403	--	--	2,403
Comprehensive income:							
Net earnings	--	--	--	31,280	--	--	31,280
Translation adjustments	--	--	--	--	1,448	--	1,448
Minimum pension liability, net of tax of $(1,103)	--	--	--	--	2,048	--	2,048
Comprehensive income							34,776
Stock options and stock compensation plans, net of tax benefit of $(3,173)	292	3	8,073	--	--	155	8,231
Balance, September 30, 2006	29,031	$290	236,390	193,046	(2,070)	(51,222)	376,434

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOW

(Dollars in thousands)

Years ended September 30,	2006	2005	2004
Cash flows from operating activities:			
Net earnings	$ 31,280	43,544	35,671
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Loss from discontinued operations, net of tax	--	--	3,737
Gain on sale of discontinued operations, net of tax	--	--	(1,592)
Asset impairment	--	790	--
Depreciation and amortization	17,303	12,184	11,888
Stock compensation expense	4,790	2,649	1,766
Changes in operating working capital	1,162	(4,634)	(2,349)
Effect of deferred taxes on tax provision	3,596	15,221	14,056
Pension contributions	(1,350)	--	(900)
Change in deferred revenue and costs, net	1,133	396	--
Other	712	(1,594)	1,485
Net cash provided by operating activities -- continuing operations	58,626	68,556	63,762
Net cash used by discontinued operations	--	--	(2,735)
Net cash provided by operating activities	58,626	68,556	61,027
Cash flows from investing activities:			
Acquisition of businesses, net of cash acquired	(91,968)	--	(294)
Proceeds from divestiture of businesses	--	--	23,275
Proceeds from note receivable	--	--	2,120
Capital expenditures -- continuing operations	(9,117)	(8,848)	(10,823)
Capital expenditures -- discontinued operations	--	--	(1,390)
Additions to capitalized software	(27,977)	(8,342)	(8,299)
Net cash provided (used) by investing activities	(129,062)	(17,190)	4,589
Cash flows from financing activities:			
Proceeds from long-term debt	52,000	--	378
Principal payments on long-term debt -- continuing operations	(52,000)	(519)	(516)
Principal payments on long-term debt -- discontinued operations	--	--	(9,024)
Net decrease in short-term borrowings	--	--	(10,000)
Purchases of common stock into treasury	--	(24,928)	(9,981)
Excess tax benefit from stock options exercised	1,569	--	--
Proceeds from exercise of stock options	2,761	3,037	3,027
Other	(1,559)	3,247	1,496
Net cash provided (used) by financing activities	2,771	(19,163)	(24,620)
Net (decrease) increase in cash and cash equivalents	(67,665)	32,203	40,996
Cash and cash equivalents at beginning of year	104,484	72,281	31,285
Cash and cash equivalents at end of year	$ 36,819	104,484	72,281
Changes in operating working capital:			
Accounts receivable, net	$ (10,029)	8,910	(8,350)
Costs and estimated earnings on long-term contracts, net	3,047	(1,916)	2,187
Inventories	1,822	(4,358)	4,145
Other current assets and current portion of deferred tax assets	737	(1,856)	(2,405)
Accounts payable	7,675	(3,156)	(2,485)
Advance payments on long-term contracts, net	594	2,468	3,161
Accrued expenses	(2,684)	(4,726)	1,398
	$ 1,162	(4,634)	(2,349)
Supplemental cash flow information:			
Interest paid	$ 456	33	402
Income taxes paid (including state, foreign & AMT)	10,768	6,269	4,974

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of ESCO Technologies Inc. (ESCO) and its wholly owned subsidiaries (the Company). All significant intercompany transactions and accounts have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform with the 2006 presentation.

B. BASIS OF PRESENTATION

Fair values of the Company's financial instruments are estimated by reference to quoted prices from market sources and financial institutions, as well as other valuation techniques. The estimated fair value of each class of financial instruments approximated the related carrying value at September 30, 2006 and 2005.

C. NATURE OF OPERATIONS

The Company has three industry operating units: Communications, Filtration/Fluid Flow and Test. The Communications unit is a proven supplier of special purpose communications systems for electric, gas and water utilities, including hardware and software to support advanced metering applications. The Filtration/Fluid Flow unit develops, manufactures and markets a broad range of filtration products used in the purification and processing of liquids and gases. The Test unit is an industry leader in providing its customers with the ability to identify, measure and contain magnetic, electromagnetic and acoustic energy.

D. USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires Management to make estimates and assumptions, including estimates of anticipated contract costs and revenues utilized in the earnings process, that affect the reported amounts of assets and liabilities and 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. Actual results could differ from those estimates.

E. REVENUE RECOGNITION

COMMUNICATIONS UNIT: Within the Communications unit, approximately 95% of the unit's revenue arrangements (approximately 30% of consolidated revenues) contain software components. Revenue under these arrangements is recognized in accordance with Statement of Position 97-2 (SOP 97-2), "Software Revenue Recognition," as amended by SOP 98-9, "Modification of SOP 97-2, Software Revenue Recognition, with Respect to Certain Transactions." The unit's software revenue arrangements generally include multiple products and services, or "elements" consisting of meter and substation hardware, meter reading system software, program management support during the deployment period and software support (post-contract customer support, "PCS"). These arrangements typically require the Company to deliver software at the inception of the arrangement while the hardware, and program management support are delivered over the contractual deployment period. Software support is provided during deployment and subsequent thereto. The software element included in such arrangements is essential to the functionality of the hardware and, therefore, the hardware is considered to be software-related. Hardware is considered a specified element in the software arrangement and vendor-specific objective evidence of fair value ("VSOE") has been established for this element. VSOE for the hardware element is determined based on the price when sold separately to customers. These revenue arrangements are divided into separate units of accounting if the delivered item(s) has value to the customer on a stand-alone basis, there is objective and reliable evidence of the fair value of the undelivered item(s) and delivery/performance of the undelivered item(s) is probable. For multiple element arrangements, revenue is allocated to the individual elements based on VSOE of the individual elements.

The application of these principles requires judgment, including the determination of whether a software arrangement includes multiple elements and estimates of the fair value of the elements. The VSOE of the undelivered elements is determined based on the historical evidence of stand-alone sales of these elements to customers. Hardware revenues are generally recognized at the time of shipment or receipt by customer depending upon contract terms. VSOE generally does not exist for the software element, therefore, the Company uses the residual method to recognize revenue when

VSOE exists for all other undelivered elements. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue.

SOP 97-2 requires the seller of software that includes post-contract customer support (PCS) to establish VSOE of the undelivered element of the contract in order to account separately for the PCS revenue. The Company determines VSOE by a consistent pricing of PCS and PCS renewals as a percentage of the software license fees or by reference to contractual renewals, when the renewal terms are substantive. Revenues for PCS are recognized ratably over the maintenance term specified in the contract (generally in 12 monthly increments). Revenues for program management support are recognized when services have been provided. The Company determines VSOE for program management support based on hourly rates when services are performed separately.

In November 2005, DCSI and Hexagram entered into arrangements with a large utility company to provide software, program management services, training and PCS that includes an option for the customer to purchase a significant quantity of hardware over an initial deployment period of approximately five years and subsequently over the remaining initial contract term of up to fifteen years. The software, program management services and training will be delivered over the initial hardware deployment period of approximately five years. PCS will be provided at no charge during the first year of the initial deployment period, after which it will be provided over subsequent annual periods throughout the contract term if the customer chooses to continue PCS. Because the program management services are based on a fixed price per month rather than on a time and materials basis, the Company is unable to establish VSOE for the program management services in this arrangement. The Company is able to establish VSOE for the PCS based on contractual renewal rates that are consistent with other arrangements and for the training based on pricing when sold separately. For the DCSI arrangement, the pricing for the optional hardware includes a discount that the Company has determined to be more-than-insignificant. In accordance with applicable software revenue recognition guidance, the Company will defer all revenue related to the DCSI arrangement until all software is delivered and acceptance criteria have been met. At that time, revenue otherwise allocable to the software, program management services, training and initial bundled PCS will be reduced by the rate of the significant incremental discount offered on the hardware products. The portion of the arrangement consideration allocated to the significant incremental discount will be recognized ratably over the discount period (up to twenty years) similar to a subscription. The remaining arrangement consideration will be recognized ratably over the period the program management services will be performed (the initial deployment period of approximately five years). Additional annual fees are payable in each subsequent year that PCS is provided and will be recognized over the respective PCS period. The amount paid by the customer for optional purchases of hardware during the deployment period related to both the DCSI and Hexagram arrangements will be recognized upon delivery and acceptance, if applicable, assuming all other revenue recognition criteria have been met.

Approximately 5% of unit revenues are recognized when products are delivered (when title and risk of ownership transfers) or when services are performed for unaffiliated customers. Products include the SecurVision(R) digital video surveillance systems.

FILTRATION/FLUID FLOW UNIT: Within the Filtration/Fluid Flow operating unit, approximately 75% of operating unit revenues (approximately 30% of consolidated revenues) are recognized when products are delivered (when title and risk of ownership transfers) or when services are performed for unaffiliated customers.

Approximately 25% of operating unit revenues (approximately 10% of consolidated revenues) are recorded under the percentage-of-completion provisions of SOP 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts." Products accounted for under SOP 81-1 include the design, development and manufacture of complex fluid control products, quiet valves, manifolds and systems primarily for the aerospace and military markets. For arrangements that are accounted for under SOP 81-1, the Company estimates profit as the difference between total estimated revenue and total estimated cost of a contract and recognizes these revenues and costs based on units delivered. The percentage-of-completion method of accounting involves the use of various techniques to estimate expected costs at completion.

TEST UNIT: Within the Test unit, approximately 60% of revenues (approximately 20% of consolidated revenues) are recognized when products are delivered (when title and risk of ownership transfers) or when services are performed for unaffiliated customers. Certain arrangements contain multiple elements which are accounted for under the provisions of EITF 00-21, "Revenue Arrangements with

Multiple Deliverables." The multiple elements generally consist of materials and installation services used in the construction and installation of standard shielded enclosures to measure and contain magnetic and electromagnetic energy. The installation process does not involve changes to the features or capabilities of the equipment and does not require proprietary information about the equipment in order for the installed equipment to perform to specifications. There is objective and reliable evidence of fair value for each of the units of accounting, as a result, the arrangement revenue is allocated to the separate units of accounting based on their relative fair values. Typically, fair value is the price of the deliverable when it is regularly sold on a stand-alone basis.

Approximately 40% of the unit's revenues (approximately 10% of consolidated revenues) are recorded under the percentage-of-completion provisions of SOP 81-1, "Accounting for the Performance of Construction-Type and Certain Production-Type Contracts" due to the complex nature of the enclosures that are designed and produced under these contracts. Products accounted for under SOP 81-1 include the construction and installation of complex test chambers to a buyer's specifications that provide its customers with the ability to measure and contain magnetic, electromagnetic and acoustic energy. As discussed above, for arrangements that are accounted for under SOP 81-1, the Company estimates profit as the difference between total estimated revenue and total estimated cost of a contract and recognizes these revenues and costs based on either (a) units delivered or (b) contract milestones.

If a reliable measure of output cannot be established (which applies in less than 8% of Test unit revenues or 2% of consolidated revenues), input measures (e.g., costs incurred) are used to recognize revenue. Given the nature of the Company's operations related to these contracts, costs incurred represent an appropriate measure of progress towards completion.

The percentage-of-completion method of accounting involves the use of various techniques to estimate expected costs at completion. These estimates are based on Management's judgment and the Company's substantial experience in developing these types of estimates.

F. CASH AND CASH EQUIVALENTS

Cash equivalents include temporary investments that are readily convertible into cash, such as Eurodollars, commercial paper and treasury bills with original maturities of three months or less.

G. ACCOUNTS RECEIVABLE

Accounts receivable have been reduced by an allowance for amounts that the Company estimates are uncollectible in the future. This estimated allowance is based on Management's evaluation of the financial condition of the customer and historical write-off experience.

H. COSTS AND ESTIMATED EARNINGS ON LONG-TERM CONTRACTS

Costs and estimated earnings on long-term contracts represent unbilled revenues, including accrued profits, accounted for under the percentage-of-completion method, net of progress billings.

I. INVENTORIES

Inventories are valued at the lower of cost (first-in, first-out) or market value. Inventories under long-term contracts reflect accumulated production costs, factory overhead, initial tooling and other related costs less the portion of such costs charged to cost of sales and any unliquidated progress payments. In accordance with industry practice, costs incurred on contracts in progress include amounts relating to programs having production cycles longer than one year, and a portion thereof will not be realized within one year.

J. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are recorded at cost. Depreciation and amortization are computed primarily on a straight-line basis over the estimated useful lives of the assets: buildings, 10-40 years; machinery and equipment, 5-10 years; and office furniture and equipment, 5-10 years. Leasehold improvements are amortized over the remaining term of the applicable lease or their estimated useful lives, whichever is shorter.

K. GOODWILL AND OTHER LONG-LIVED ASSETS

Goodwill represents the excess of purchase costs over the fair value of net identifiable assets acquired in business acquisitions. The Company accounts for goodwill as required by Statement of Financial Accounting Standards (SFAS) 142, "Goodwill and Other Intangible Assets." Management annually reviews goodwill and other long-lived assets with indefinite useful lives for impairment or whenever events or changes in circumstances indicate the carrying amount may not be recoverable.

If the Company determines that the carrying value of the long-lived asset may not be recoverable, a permanent impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value. Fair value is measured based on a discounted cash flow method using a discount rate determined by Management to be commensurate with the risk inherent in the Company's current business model. Other intangible assets represent costs allocated to identifiable intangible assets, principally capitalized software, patents, trademarks, and technology rights. See Note 5 regarding goodwill and other intangible assets activity.

L. CAPITALIZED SOFTWARE

The costs incurred for the development of computer software that will be sold, leased, or otherwise marketed are charged to expense when incurred as research and development until technological feasibility has been established for the product. Technological feasibility is typically established upon completion of a detailed program design. Costs incurred after this point are capitalized on a project-by-project basis in accordance with SFAS No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed." Costs that are capitalized primarily consist of external development costs. Upon general release of the product to customers, the Company ceases capitalization and begins amortization, which is calculated on a project-by-project basis as the greater of (1) the ratio of current gross revenues for a product to the total of current and anticipated future gross revenues for the product or (2) the straight-line method over the estimated economic life of the product. The Company generally amortizes the software development costs over a three to seven year period based upon the estimated future economic life of the product. Factors considered in determining the estimated future economic life of the product include anticipated future revenues, and changes in software and hardware technologies. The carrying values of capitalized costs are evaluated for impairment on an annual basis to determine if circumstances exist which indicate the carrying value of the asset may not be recoverable. If expected cash flows are insufficient to recover the carrying amount of the asset, then an impairment loss is recognized to state the asset at its net realizable value.

M. IMPAIRMENT OF LONG-LIVED ASSETS AND LONG-LIVED ASSETS TO BE DISPOSED OF

Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to dispose.

N. INCOME TAXES

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets may be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax assets will not be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company regularly reviews its deferred tax assets for recoverability and establishes a valuation allowance when Management believes it is more likely than not such assets will not be recovered, taking into consideration historical operating results, expectations of future earnings, tax planning strategies, and the expected timing of the reversals of existing temporary differences.

O. RESEARCH AND DEVELOPMENT COSTS

Company-sponsored research and development costs include research and development and bid and proposal efforts related to the Company's products and services. Company-sponsored product development costs are charged to expense when incurred. Customer-sponsored research and development costs incurred pursuant to contracts are accounted for similar to other program costs. Customer-sponsored research and development costs refer to certain situations whereby customers provide funding to support specific contractually defined research and development costs. As the Company incurs costs under these specific funding contracts, the costs are "inventoried" until billed to the customer for reimbursement, consistent with other program costs. Once billed/invoiced, these costs are transferred to accounts receivable until the cash is received from the customer. All research and development costs incurred in excess of the contractual funding amount, or costs incurred outside the scope of the contractual research and development project, are expensed as incurred.

P. FOREIGN CURRENCY TRANSLATION

The financial statements of the Company's foreign operations are translated into U.S. dollars in accordance with SFAS 52 "Foreign Currency Translation" (SFAS 52). The resulting translation adjustments are recorded as a separate component of accumulated other comprehensive income.

Q. EARNINGS PER SHARE

Basic earnings per share is calculated using the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated using the weighted average number of common shares outstanding during the period plus shares issuable upon the assumed exercise of dilutive common share options and vesting of performance-accelerated restricted shares using the treasury stock method. On August 5, 2005, the Company's Board of Directors approved a 2-for-1 stock split which was effected as a 100 percent stock dividend and was paid on September 23, 2005 to shareholders of record as of September 9, 2005. The 2004 common stock and per share amounts have been adjusted to reflect the stock split.

The number of shares used in the calculation of earnings per share for each year presented is as follows:

(In thousands)	2006	2005	2004
Weighted Average Shares Outstanding -- Basic	25,718	25,511	25,803
Dilutive Options and performance-accelerated restricted stock	668	795	845
Adjusted Shares -- Diluted	26,386	26,306	26,648

Options to purchase 264,430 shares at prices ranging from $42.99 - $54.88 were outstanding during the year ended September 30, 2006, but were not included in the respective computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares. Options to purchase 34,967 shares at prices ranging from $35.18 - $50.26 were outstanding during the year ended September 30, 2005, but were not included in the respective computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares. Options to purchase 212,228 shares at prices ranging from $22.68 - $32.33 were outstanding during the year ended September 30, 2004, but were not included in the respective computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares. These options expire in various periods through 2013. Approximately 9,000, 36,000 and 14,000 restricted shares were outstanding but unearned at September 30, 2006, 2005 and 2004, respectively, and, therefore, were not included in the respective years' computations of diluted EPS.

R. SHARE-BASED COMPENSATION

Prior to October 1, 2005, the Company accounted for its stock option plans using the intrinsic value method of accounting provided under APB Opinion No. 25, "Accounting for Stock Issued to Employees," (APB 25) and related interpretations, as permitted by FASB Statement No. 123, "Accounting for Stock-Based Compensation," (SFAS 123) under which no compensation expense was recognized for stock option grants. Accordingly, share-based compensation for stock options was included as a pro forma disclosure in the financial statement footnotes for periods prior to fiscal 2006.

Effective October 1, 2005, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), "Share-Based Payment," (SFAS 123(R)) using the modified-prospective transition method. Under this transition method, compensation cost recognized in fiscal 2006 includes:

a) compensation cost for all share-based payments granted through September 30, 2005, for which the requisite service period had not been completed as of September 30, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and

b) compensation cost for all share-based payments granted subsequent to September 30, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). Results for prior periods have not been restated.

As a result of adopting SFAS 123(R) on October 1, 2005, the Company's net earnings for the year ended September 30, 2006 were $2.3 million lower than if it had continued to account for share-based compensation under APB 25.

The Company has various share-based plans which allow the Company to grant key officers, managers and professional employees (1) options to purchase shares of the Company's common stock, (2) stock appreciation rights with respect to all or any part of the number of shares covered by the options, or (3) performance-accelerated restricted shares (restricted shares) and other full value awards. No stock appreciation rights have been awarded to date. In addition, the Company provides compensation benefits to non-employee directors under a non-employee directors compensation plan.

S. COMPREHENSIVE INCOME (LOSS)

SFAS 130, "Reporting Comprehensive Income" requires the Company to report separately the translation adjustments of SFAS 52 defined above, and changes to the minimum pension liability, as components of comprehensive income or loss. Management has chosen to disclose the requirements of this Statement within the Consolidated Statements of Shareholders' Equity.

Accumulated other comprehensive loss as shown on the consolidated balance sheet of $(2.1) million and $(5.6) million at September 30, 2006 and 2005, respectively, consisted of $4.5 million and $3.0 million related to currency translation adjustments; $(6.6) million and $(8.6) million related to the minimum pension liability, respectively.

T. DEFERRED REVENUE

Deferred revenue is recorded for products or services that have not been provided but have been invoiced under contractual agreements or paid for by a customer, or when products or services have been provided but the criteria for revenue recognition have not been met. If there is a customer acceptance provision or there is uncertainty about customer acceptance, revenue is deferred until the customer has accepted the product or service. The current portion of approximately $3.0 million is classified in accrued expenses on the Consolidated Balance Sheet.

Deferred revenue also includes the long-term portion of unearned income related to two intellectual property agreements. The amount is being amortized into income on a straight-line basis over the remaining patent life through 2011. The current portion of approximately $0.6 million is classified in accrued expenses on the Consolidated Balance Sheet.

U. NEW ACCOUNTING STANDARDS

In December 2004, the FASB issued SFAS No. 123(R), "Share-Based Payment" (SFAS 123(R)). This Statement replaces SFAS No. 123, "Accounting for Stock-Based Compensation" and supersedes APB No. 25, "Accounting for Stock Issued to Employees." SFAS 123(R) requires all stock-based compensation to be recognized as an expense in the financial statements and that such cost be measured according to the fair value of stock options. The Company adopted the provisions of this Statement in the first quarter of fiscal 2006 on a prospective basis.

In December 2004, the FASB issued FASB Staff Position FAS 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" (FSP 109-2). The American Jobs Creation Act of 2004, (the "Act") provides for a special one-time deduction of 85 percent of certain foreign earnings repatriated into the U.S. from non-U.S. subsidiaries through September 30, 2006. During fiscal 2006, the Company repatriated $39.5 million of foreign earnings which qualify for the special one-time deduction. Tax expense of $2.4 million was recorded in fiscal 2006 as a result of this repatriation.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109." This Interpretation is effective for ESCO beginning October 1, 2007. This Interpretation prescribes a recognition threshold and measurement process for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company is currently evaluating the adoption of this Interpretation and does not currently have an estimate of the impact on the consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158, "Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158), which amends SFAS 87 and SFAS 106 to require recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. Under SFAS 158, gains and losses, prior service costs and credits, and any remaining transition amounts under SFAS 87 and SFAS 106 that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects. The measurement date -- the date at which the benefit obligation and plan assets are measured -- is required to be the Company's fiscal year-end, which is the date the Company currently uses. SFAS 158 is effective for publicly-held companies for fiscal years ending after December 15, 2006. The adoption of SFAS 158 is not expected to have a material impact to the Company's financial position or results of operations.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB No. 108), which addresses the diversity in practice in quantifying financial statement misstatements and provides interpretative guidance regarding the consideration given to prior year misstatements when determining materiality in current year financial statements. During 2006, the Company adopted the provisions of SAB No. 108 and recorded $2.4 million as a cumulative credit adjustment to 2006 beginning retained earnings.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" (SFAS 157), which defines fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS 157 is not expected to have a material impact to the Company's financial position or results of operations.

2. ACQUISITIONS

Effective February 1, 2006, the Company acquired the capital stock of Hexagram, Inc. (Hexagram) for a purchase price of approximately $66 million. The acquisition agreement also provides for contingent consideration of up to $6.25 million over the five year period following the acquisition if Hexagram exceeds certain sales targets. Hexagram is an RF fixed network automatic meter reading (AMR) company headquartered in Cleveland, Ohio. Hexagram broadens the Company's served market and provides an RF based AMI system serving primarily gas and water utilities. Hexagram's annual revenue over the past three years has been in the range of $20 million to $35 million. The operating results for Hexagram, since the date of acquisition, are included within the Communications unit. The Company recorded $6.6 million of amortizable identifiable intangible assets consisting primarily of patents and proprietary know-how, customer contracts, and order backlog which are being amortized on a straight-line basis over periods ranging from six months to seven years.

The following table summarizes the Company's estimates of the fair values of the assets acquired and liabilities assumed at the date of acquisition and includes subsequent adjustments to the allocation of purchase price.

Hexagram, Inc.
Assets Acquired and Liabilities Assumed
February 1, 2006

(Dollars in thousands)

Cash	$ 2,128
Accounts receivable, net	3,267
Inventory	4,161
Other current assets	276
Property, plant and equipment	2,223
Deferred tax assets	735
Other assets	60
Intangible assets:	
Trademarks	3,485
Patents	3,468
Customer contracts	2,378
Other	727
	10,058
Goodwill	51,202
Current liabilities	(4,149)
Deferred tax liabilities	(3,774)
Other long-term liabilities	(116)
Aggregate purchase price	$66,071

Effective November 29, 2005, the Company acquired Nexus Energy Software, Inc. (Nexus) through an all cash for shares merger transaction for approximately $29 million in cash plus contingent cash consideration over the four year period following the merger if Nexus exceeds certain sales targets. Nexus is a software company headquartered in Wellesley, Massachusetts with annual revenues in the past in excess of $10 million. Nexus broadens the Company's served market and provides software solutions that allow utilities to fully utilize the information produced by the Company's AMI systems. The operating results for Nexus, since the date of acquisition, are included within the Communications unit. The Company recorded $2.7 million of identifiable intangible assets consisting primarily of customer contracts and order backlog which are being amortized on a straight-line basis over periods ranging from one year to three years. In connection with the acquisition of Nexus, the Company acquired approximately $13 million of net operating loss carryforward that will expire between 2017 and 2025 and is subject to a Section 382 limitation.

The following table summarizes the Company's estimates of the fair values of the assets acquired and liabilities assumed at the date of acquisition and includes subsequent adjustments to the allocation of purchase price.

Nexus Energy Software, Inc.
Assets Acquired and Liabilities Assumed
November 29, 2005

(Dollars in thousands)

Cash	$ 440
Accounts receivable, net	1,701
Other current assets	228
Property, plant and equipment	965
Deferred tax assets	4,469
Other assets	176
Intangible assets:	
Contracts/software	1,497
Backlog	1,064
Other	162
	2,723
Goodwill	23,434
Current liabilities	(3,862)

Deferred tax liabilities	(1,095)
Other long-term liabilities	(180)
Aggregate purchase price	$28,999

All of the Company's acquisitions have been accounted for using the purchase method of accounting and accordingly, the respective purchase prices were allocated to the assets (including intangible assets) acquired and liabilities assumed based on estimated fair values at the date of acquisition. The financial results from these acquisitions have been included in the Company's financial statements from the date of acquisition. Pro forma financial information related to the Nexus and Hexagram acquisitions was not presented as it was not significant to the Company's results of operations. None of the goodwill recorded as part of the Nexus or Hexagram acquisitions is expected to be deductible for U.S. federal or state income tax purposes.

3. DISCONTINUED OPERATIONS

The MicroSep businesses consisted of PTI Advanced Filtration Inc., PTI Technologies Limited, and PTI S.p.A. Effective April 2, 2004, the Company completed the sale of PTI Advanced Filtration Inc. (Oxnard, California) and PTI Technologies Limited (Sheffield, England) to domnick hunter group plc for $18 million in cash. On June 8, 2004, the Company completed the sale of PTI S.p.A. (Milan, Italy) to a group of investors comprised of the subsidiary's senior management for $5.3 million. An after-tax gain of $1.6 million related to the sale of the MicroSep businesses is reflected in the Company's 2004 results in discontinued operations.

The MicroSep businesses are accounted for as a discontinued operation in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144) and, accordingly, amounts in the financial statements and related notes for all periods shown, reflect discontinued operations presentation. The net sales from the MicroSep businesses were $29.4 million for the year ended September 30, 2004. The pre-tax loss from operations from the MicroSep businesses was $5.0 million for the year ended September 30, 2004.

4. ASSET IMPAIRMENT

In June 2005, the Company abandoned its plans to commercialize certain sensor products within the Filtration/Fluid Flow segment. This action resulted in an asset impairment charge of $0.8 million to write off certain patents and a related licensing agreement to their respective fair market values. The Company ended its development efforts on this program after it determined that the market was not developing as quickly as anticipated and the expected costs and time frame to fully commercialize the products were not acceptable.

5. GOODWILL AND OTHER INTANGIBLE ASSETS

Included on the Company's Consolidated Balance Sheet at September 30, 2006 and 2005 are the following intangible assets gross carrying amounts and accumulated amortization:

(Dollars in millions)	2006	2005
Goodwill:		
Gross carrying amount	$152.4	77.8
Less: accumulated amortization	8.9	8.9
Net	$143.5	68.9
Intangible assets with determinable lives:		
Patents		
Gross carrying amount	$ 17.6	17.5
Less: accumulated amortization	13.9	13.1
Net	$ 3.7	4.4
Capitalized software		
Gross carrying amount	$ 55.3	23.9
Less: accumulated amortization	10.1	6.8

Net	$ 45.2	17.1
Other		
Gross carrying amount	$ 9.5	0.4
Less: accumulated amortization	2.8	0.3
Net	$ 6.7	0.1
Intangible assets with indeterminable lives:		
Trademarks	$ 3.5	--

The Company performed its annual evaluation of goodwill for impairment during the fourth quarter of fiscal 2006 and concluded no impairment existed at September 30, 2006. The changes in the carrying amount of goodwill attributable to each business segment for the years ended September 30, 2006 and 2005 are as follows:

(Dollars in millions)	Communications	Filtration/ Fluid Flow	Test
Balance as of September 30, 2005	$ --	39.8	29.1
Acquisitions (Hexagram and Nexus)	74.6	--	--
Balance as of September 30, 2006	$74.6	39.8	29.1

Amortization expense related to intangible assets with determinable lives was $6.9 million, $2.0 million and $2.1 million in 2006, 2005 and 2004, respectively. The increase in amortization expense in 2006 as compared to the prior year was due to $2.7 million of amortization related to the Nexus and Hexagram acquired intangible assets and $2.2 million of amortization related to the Company's TNG software. Patents are amortized over the life of the patents, generally 17 years. Capitalized software is amortized over the estimated useful life of the software, generally 3-7 years. Estimated intangible assets amortization for fiscal year 2007 is approximately $11 million. Estimated intangible asset amortization for fiscal years 2008 through 2011 is estimated at approximately $12 million to $13 million per year. The increase in intangible asset amortization is related to the additional costs associated with the TNG software.

6. ACCOUNTS RECEIVABLE

Accounts receivable, net of the allowance for doubtful accounts, consist of the following at September 30, 2006 and 2005:

(Dollars in thousands)	2006	2005
Commercial	$81,986	66,871
U.S. Government and prime contractors	1,830	1,948
Total	$83,816	68,819

7. INVENTORIES

Inventories consist of the following at September 30, 2006 and 2005:

(Dollars in thousands)	2006	2005
Finished goods	$12,834	14,361
Work in process -- including long-term contracts	13,211	12,512
Raw materials	24,939	21,772
Total	$50,984	48,645

8. PROPERTY, PLANT AND EQUIPMENT

Depreciation expense from continuing operations of property, plant and equipment for the years ended September 30, 2006, 2005 and 2004 was $10.4 million, $10.1 million and $9.5 million, respectively.

The closure and relocation of the Filtertek Puerto Rico facility was completed in March 2004. The Puerto Rico facility is included in other current assets with a carrying value of $3.6 million at September 30, 2006. The facility is being marketed for sale.

The Company leases certain real property, equipment and machinery under noncancelable operating leases. Rental expense under these operating leases for the years ended September 30, 2006, 2005 and 2004 was $7.3 million, $6.3 million and $5.8 million, respectively. Future aggregate minimum lease payments under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of September 30, 2006 are:

(Dollars in thousands)

Years ending September 30:	
2007	$ 7,112
2008	4,789
2009	3,128
2010	2,310
2011 and thereafter	4,935
Total	$22,274

9. INCOME TAX EXPENSE

Total income tax expense for the years ended September 30, 2006, 2005 and 2004 was allocated as follows:

(Dollars in thousands)	2006	2005	2004
Income tax expense from continuing operations	$17,622	20,363	22,748
Discontinued operations	--	--	(2,481)
Total income tax expense	$17,622	20,363	20,267

For the year ended September 30, 2006, pretax earnings related to United States (U.S.) and foreign tax jurisdictions were $43.9 million and $5.0 million, respectively. For the year ended September 30, 2005, pretax earnings related to U.S. and foreign tax jurisdictions were $52.5 million and $11.4 million, respectively. For the year ended September 30, 2004, pretax earnings related to U.S. and foreign tax jurisdictions was $46.3 million and $9.6 million, respectively.

The principal components of income tax expense from continuing operations for the years ended September 30, 2006, 2005 and 2004 consist of:

(Dollars in thousands)	2006	2005	2004
Federal			
Current (including Alternative Minimum Tax)	$ 3,571	874	14,153
Deferred	10,291	15,313	3,641
State and local:			
Current	2,673	2,414	3,259
Deferred	(518)	(21)	76
Foreign:			
Current	1,213	1,854	1,752
Deferred	392	(71)	(133)
Total	$17,622	20,363	22,748

The actual income tax expense from continuing operations for the years ended September 30, 2006, 2005 and 2004 differs from the expected tax expense for those years (computed by applying the U.S. Federal corporate statutory rate) as follows:

	2006	2005	2004
Federal corporate statutory rate	35.0%	35.0%	35.0%
State and local, net of Federal benefits	2.4	2.4	3.5
Foreign -- Puerto Rico	0.5	(4.6)	(3.1)
Foreign -- Other	(0.5)	(1.6)	--
Foreign earnings repatriation	4.8	--	--
Research credit	(5.0)	--	--
SFAS 123(R)	1.4	--	--
Change in tax contingencies	(2.9)	--	--

Other, net	0.3	0.7	2.2
Effective income tax rate	36.0%	31.9%	37.6%

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at September 30, 2006, and 2005 are presented below.

(Dollars in thousands)	2006	2005
Deferred tax assets:		
Inventories, long-term contract accounting, contract cost reserves and others	$ 1,858	3,159
Pension and other postretirement benefits	5,449	6,981
Net operating loss carryforward -- domestic	5,103	15,695
Net operating loss carryforward -- foreign	2,895	1,715
Capital loss carryforward	7,381	7,381
Other compensation-related costs and other cost accruals	18,484	11,687
Research credit carryforward	6,635	--
Total deferred tax assets	47,805	46,618
Deferred tax liabilities:		
Plant and equipment, depreciation methods, acquisition asset allocations, and other	(17,028)	(12,926)
Net deferred tax asset before valuation allowance	30,777	33,692
Less valuation allowance	(10,276)	(9,096)
Net deferred tax assets	$ 20,501	24,596

Net deferred tax assets are classified in the Consolidated Balance Sheets as set forth below.

(Dollars in thousands)	2006	2005
Current portion of deferred tax assets	$24,251	25,271
Deferred tax liabilities (non-current) -- Included in Other Liabilities	(3,750)	(675)
Net deferred tax assets	$20,501	24,596

Management believes that, based on the Company's historical pretax income together with the projection of future taxable income, and after consideration of the valuation allowance, it is more likely than not that the Company will realize the benefits of the net deferred tax assets existing at September 30, 2006. In order to realize this net deferred tax asset, the Company will need to generate future taxable income of approximately $59 million, of which $15 million is required to be realized prior to the expiration of the NOL carryforward in the United States. The expiration of the NOL carryforward is between 2019 and 2025. The Company anticipates being able to utilize the NOL carryforward to reduce future Federal income tax cash payments.

The Company has established a valuation allowance of $7.4 million against the capital loss carryforward generated in 2004, as such loss carryforward may not be realized in future periods. In addition, the Company has established a valuation allowance against certain NOL carryforwards in foreign jurisdictions which may not be realized in future periods. The valuation allowance established against the foreign NOL carryforwards was $2.9 million and $1.7 million at September 30, 2006 and 2005, respectively. The Company classifies its valuation allowance related to deferred taxes on a pro rata basis. The Company reclassified the current and long-term portion of its valuation allowance as of September 30, 2005 to be consistent with the current year presentation.

On October 22, 2004, the President of the United States signed into law the American Jobs Creation Act of 2004 (the "2004 Jobs Act"). The 2004 Jobs Act repeals the extraterritorial income exclusion and provides for (i) a new deduction for domestic manufacturing and production income, (ii) international tax reforms, (iii) a temporary incentive for U.S. multinational companies to reinvest foreign earnings in the U.S., and (iv) numerous other business tax relief provisions. The foreign earnings repatriation provision provides an 85% dividends received deduction for certain dividends received from controlled foreign corporations. In addition, in December 2004, the FASB issued FASB Staff Position FAS 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" (2004 Jobs Act). The Company repatriated $39.5 million of funds to reinvest in the U.S. under the 2004 Jobs Act. Federal income taxes on the repatriated amounts were based on the 5.25% effective statutory rate as provided in the 2004 Jobs Act, plus applicable state income and foreign withholding taxes. Federal income taxes and applicable withholding taxes of $2.4 million have been provided for in the current year provision.

Under current law, the research credit expired for research expenditures incurred after December 31, 2005. The Company began an analysis of available research credits for the period beginning in 2000 and ending with the three month period ended December 31, 2005. The Company expects that these research credit claims will be approximately $2.5 million.

No deferred taxes have been provided on the accumulated unremitted earnings of the Company's foreign subsidiaries as of September 30, 2006. The Company's intention is to reinvest these earnings indefinitely. In the event these foreign entities' earnings were distributed, it is estimated that U.S. taxes, net of available foreign tax credits, of approximately $3.2 million would be due, which would correspondingly reduce the Company's net earnings.

During 2006, the Company determined that state tax expense had not been accurately recorded in the financial statements for years 2001 through 2005. The effect in any individual prior year was not material to the Company's results of operations, financial position or cash flows. The Company adopted the provisions of SEC Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" and recorded $2.4 million as a cumulative credit adjustment to 2006 beginning retained earnings.

The Company operates within multiple taxing jurisdictions and is subject to audit in these jurisdictions. These audits can involve complex issues which may require an extended period of time to resolve. The Company regularly reviews its potential tax liabilities for tax years subject to audit. Changes in the Company's potential tax liability occurred during the year ended September 30, 2006, and may occur in the future as the Company's assessment changes based on examinations in various jurisdictions and/or changes in tax laws, regulations and case law. Accordingly, the Company's estimate of income tax liabilities may differ from actual payments or assessments.

10. DEBT

At September 30, 2006 and 2005, there were no outstanding borrowings under the revolving credit facility. Effective October 6, 2004, the Company entered into a $100 million five-year revolving bank credit facility with a $50 million increase option that has a final maturity and expiration date of October 6, 2009. The credit facility is available for direct borrowings and/or the issuance of letters of credit, and is provided by a group of six banks, led by Wells Fargo Bank as agent. At September 30, 2006, the Company had approximately $99.2 million available to borrow under the credit facility in addition to $36.8 million cash on hand. At September 30, 2006, the Company had outstanding letters of credit of $1.5 million ($0.8 million outstanding under the credit facility). On February 1, 2006, the Company borrowed $47 million to partially fund the acquisition of Hexagram which was subsequently repaid from the foreign cash repatriation by March 31, 2006. The interest rate on this debt was approximately 5.3%. During April 2006, the Company borrowed $5 million which was subsequently repaid prior to April 30, 2006. The interest rate on this debt was 7.75%.

The credit facility requires, as determined by certain financial ratios, a commitment fee ranging from 17.5 to 27.5 basis points per annum on the unused portion. The terms of the facility provide that interest on borrowings may be calculated at a spread over the London Interbank Offered Rate (LIBOR) or based on the prime rate, at the Company's election. The facility is secured by the unlimited guaranty of the Company's material domestic subsidiaries and a 65% pledge of the material foreign subsidiaries' share equity. The financial covenants of the credit facility include limitations on leverage, minimum consolidated EBITDA and minimum net worth.

During 2006 and 2005, the maximum aggregate short-term borrowings at any month-end were $47 million and zero, respectively; the average aggregate short-term borrowings outstanding based on month-end balances were $3.9 million and zero, respectively; and the weighted average interest rates were 5.25%, not applicable in 2005, and 1.87% in 2004. The letters of credit issued and outstanding under the credit facility totaled $0.8 million and $1.4 million at September 30, 2006, and 2005, respectively.

11. CAPITAL STOCK

The 29,030,995 and 28,738,958 common shares as presented in the accompanying Consolidated Balance Sheets at September 30, 2006 and 2005 represent the actual number of shares issued at the respective dates. The Company held 3,166,026 and 3,175,626 common shares in treasury at September 30, 2006 and 2005, respectively.

In August 2006, the Company's Board of Directors authorized an open market common stock repurchase program for up to 1.2 million shares, subject to market conditions and other factors which covers the period through September 30, 2008. There were no stock repurchases during fiscal 2006. The Company repurchased 670,072 and 312,400 shares in 2005 and 2004, respectively, under a previously authorized program.

12. SHARE-BASED COMPENSATION

Prior to October 1, 2005, the Company accounted for its stock option plans using the intrinsic value method of accounting provided under APB Opinion No. 25, "Accounting for Stock Issued to Employees," (APB 25) and related interpretations, as permitted by FASB Statement No. 123, "Accounting for Stock-Based Compensation," (SFAS 123) under which no compensation expense was recognized for stock option grants. Accordingly, share-based compensation for stock options was included as a pro forma disclosure in the financial statement footnotes for periods prior to fiscal 2006.

Effective October 1, 2005, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), "Share-Based Payment," (SFAS 123(R)) using the modified-prospective transition method. Under this transition method, compensation cost recognized in fiscal 2006 includes:

c) compensation cost for all share-based payments granted through September 30, 2005, for which the requisite service period had not been completed as of September 30, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and

d) compensation cost for all share-based payments granted subsequent to September 30, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). Results for prior periods have not been restated.

As a result of adopting SFAS 123(R) on October 1, 2005, the Company's net earnings for the year ended September 30, 2006 were $2.3 million lower than if it had continued to account for share-based compensation under APB 25.

The Company has various share-based plans which allow the Company to grant key officers, managers and professional employees (1) options to purchase shares of the Company's common stock, (2) stock appreciation rights with respect to all or any part of the number of shares covered by the options, or (3) performance-accelerated restricted shares and other stock based awards. No stock appreciation rights have been awarded to date. In addition, the Company provides compensation benefits to non-employee directors under a non-employee directors compensation plan. During fiscal 2004, the Board of Directors authorized and the shareholders approved, the 2004 Incentive Compensation Plan, which states, in part, that on February 5, 2004, there shall be added to the authorized shares allocated 2,000,000 shares for the grant of stock options, stock appreciation rights, performance-accelerated restricted stock, or other full value awards. Of these, shares up to 600,000 may be utilized for performance-accelerated restricted stock or other full value awards. At September 30, 2006, the maximum number of full value shares available for issue under the 2004 Incentive Compensation Plan and the 2001 Stock Incentive Plan was 600,000 and 330,032 shares, respectively.

STOCK OPTION PLANS

The Company's stock option awards are generally subject to graded vesting over a three year service period. All outstanding options were granted at prices equal to fair market value at the date of grant. The options granted prior to September 30, 2003 have a ten-year contractual life from date of issuance, expiring in various periods through 2013. Beginning in fiscal 2004, the options granted have a five-year contractual life from date of issuance. Beginning with fiscal 2006 awards, the Company recognizes compensation cost on a straight-line basis over the requisite service period for the entire award. Prior to fiscal 2006, the Company calculated the pro forma compensation cost using the graded vesting method (FIN 28 approach).

The fair value of each option award is estimated as of the date of grant using a Black-Scholes option pricing model. The weighted average assumptions for the periods indicated are noted below. Expected volatility is based on historical volatility of ESCO's stock calculated over the expected term of the option. The expected term was calculated in accordance with Staff Accounting Bulletin No. 107 using the simplified method for "plain-vanilla" options. The risk-free rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the date of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 2006, 2005 and 2004, respectively: expected dividend yield of 0% in all periods; expected volatility of 28.0%, 23.5% and 21.4%; risk-free interest rate of 4.6%, 3.9% and 4.2%; and expected term of 3.50 years, 3.58 years and 4.25 years.

Information regarding stock options awarded under the option plans is as follows:

	FY2006		FY2005		FY2004	
	SHARES	ESTIMATED WEIGHTED AVG. PRICE	Shares	Estimated Weighted Avg. Price	Shares	Estimated Weighted Avg. Price
October 1	1,324,548	$20.48	1,356,094	$13.63	1,529,192	$10.89
Granted	328,080	$44.63	376,200	$35.55	291,600	$24.15
Exercised	(232,371)	$15.95	(388,340)	$10.94	(385,166)	$10.13
Cancelled	(32,909)	$35.77	(19,406)	$24.96	(79,532)	$16.26
September 30,	1,387,348	$26.60	1,324,548	$20.48	1,356,094	$13.63
At September 30,						
Reserved for future grant	1,146,741		1,428,032		1,665,238	
Exercisable	753,415	$16.46	755,612	$12.29	818,824	$ 9.71

The aggregate intrinsic value of options exercised during 2006, 2005 and 2004 was $7.9 million, $12.4 million and $6.2 million, respectively. The aggregate intrinsic value of stock options outstanding and exercisable at September 30, 2006 was $32.1 million and $22.7 million, respectively. The weighted-average contractual life of stock options outstanding at September 30, 2006 was 3.75 years. The weighted-average fair value of stock options granted in 2006, 2005, and 2004 was $12.17, $11.28, and $6.84, respectively.

Summary information regarding stock options outstanding at September 30, 2006 is presented below:

	Options Outstanding		
Range of Exercise Prices	Number Outstanding at Sept. 30, 2006	Weighted-Average Remaining Contractual Life	Weighted Average Exercise Price
$ 4.59 - $10.72	215,244	3.0 years	$ 7.21
$12.59 - $14.52	292,912	5.5 years	$13.71
$17.16 - $32.32	229,371	2.7 years	$23.34
$35.18 - $42.10	327,241	3.0 years	$35.29
$42.99 - $54.88	322,580	4.2 years	$44.74
	1,387,348	3.8 years	$26.60

	Exercisable Options Outstanding	
Range of Exercise Prices	Number Exercisable at Sept. 30, 2006	Weighted Average Exercise Price
$ 4.59 - $10.72	215,244	$ 7.21
$12.59 - $14.52	292,912	$13.71
$17.16 - $32.32	148,150	$22.88
$35.18 - $50.10	97,109	$35.42
	753,415	$16.46

PERFORMANCE-ACCELERATED RESTRICTED SHARE AWARDS

The performance-accelerated restricted shares (restricted shares) vest over five years with accelerated vesting if certain performance targets are achieved. In these cases, if it is probable that the performance condition will be met, the Company recognizes compensation cost on a straight-line basis over the shorter performance period; otherwise, it will recognize compensation cost over the longer service period. Compensation cost for all outstanding restricted share awards is being recognized over the shorter performance period as it is probable the performance condition will be met. The restricted share award grants were valued at the stock price on the date of grant. Pre-tax compensation expense related to the restricted share awards was $1.5 million, $1.9 million and $1.4 million for fiscal years ended September 30, 2006, 2005 and 2004, respectively.

The following summary presents information regarding outstanding restricted share awards as of September 30, 2006 and changes during the period then ended:

	Shares	Weighted Avg. Price
Nonvested at October 1, 2005	238,436	$23.78
Granted	64,130	$43.02
Vested	(118,736)	$17.41
Cancelled	(28,100)	$36.16
Nonvested at September 30, 2006	155,730	$34.33

NON-EMPLOYEE DIRECTORS PLAN

The non-employee directors compensation plan provides to each non-employee director a retainer of 800 common shares per quarter. Compensation expense related to the non-employee director grants was $1.0 million, $0.7 million and $0.4 million for the years ended September 30, 2006, 2005 and 2004, respectively.

The total share-based compensation cost that has been recognized in results of operations and included within SG&A was $4.8 million, $2.6 million and $1.8 million for the years ended September 30, 2006, 2005 and 2004, respectively. The total income tax benefit recognized in results of operations for share-based compensation arrangements was $1.2 million, $1.0 million and $0.7 million for the years ended September 30, 2006, 2005 and 2004, respectively. The Company has elected to use tax law ordering rules when calculating the income tax benefit associated with its share-based payment arrangements. In addition, the Company elected to use the simplified method of calculating the pool of excess tax benefits available to absorb tax deficiencies recognized subsequent to the adoption of SFAS No. 123(R)-3, "Transition Election related to Accounting for the Tax Effects of Share-Based Payment Awards." As of September 30, 2006, there was $8.4 million of total unrecognized compensation cost related to share-based compensation arrangements. That cost is expected to be recognized over a weighted-average period of 3.5 years.

PRO FORMA NET EARNINGS

The following table provides pro forma net earnings and earnings per share had the Company applied the fair value method of SFAS 123 for the years ended September 30, 2005 and 2004:

Pro forma (Unaudited)

(Dollars in thousands, except per share amounts)	2005	2004
Net earnings, as reported	$43,544	35,671
Add: stock-based employee compensation expense included in reported net earnings, net of tax	1,165	866
Less: total stock-based employee compensation expense determined under fair value based methods, net of tax	(3,476)	(1,910)
Pro forma net earnings	$41,233	34,627
Net earnings per share:		
Basic -- as reported	$ 1.71	1.38
Basic -- pro forma	1.62	1.34
Diluted -- as reported	1.66	1.34
Diluted -- pro forma	1.57	1.30

13. RETIREMENT AND OTHER BENEFIT PLANS

Substantially all employees are covered by defined contribution pension plans maintained by the Company for the benefit of its employees. Effective December 31, 2003, the Company's defined benefit plan was frozen and no additional benefits will be accrued after that date. As a result, the accumulated benefit obligation and projected benefit obligation are equal. These frozen retirement income benefits are provided to employees under defined benefit pay-related and flat-dollar plans, which are noncontributory. The annual contributions to retirement plans equal or exceed the minimum funding requirements of the Employee Retirement Income Security Act or applicable local regulations. In addition to providing retirement income benefits, the Company provides unfunded postretirement health and life insurance benefits to certain retirees. To qualify, an employee must retire at age 55 or later and the employee's age plus service must equal or exceed 75. Retiree contributions are defined as a percentage of medical premiums. Consequently, retiree contributions increase with increases in the medical premiums. The life insurance plans are noncontributory and provide coverage of a flat dollar amount for qualifying retired employees.

The Company uses a measurement date of September 30 for its pension and other postretirement benefit plans. The Company has an accrued benefit liability of $1.8 million and $1.9 million at September 30, 2006 and 2005, respectively, related to its other postretirement benefit obligations. All other information related to its postretirement benefit plans is not considered material to the Company's results of operations or financial condition.

The following tables provide a reconciliation of the changes in the pension plans and fair value of assets over the two-year period ended September 30, 2006, and a statement of the funded status as of September 30, 2006 and 2005:

(Dollars in millions)	Pension Benefits 2006	2005
RECONCILIATION OF BENEFIT OBLIGATION		
Net benefit obligation at beginning of year	$50.2	45.0
Service cost	--	--
Interest cost	2.6	2.6
Actuarial (gain) loss	(2.9)	4.2
Plan amendments	0.1	--
Plan participant contributions	--	--
Gross benefits paid	(1.8)	(1.6)
Net benefit obligation at end of year	$48.2	50.2

(Dollars in millions)	Pension Benefits 2006	2005
RECONCILIATION OF FAIR VALUE OF PLAN ASSETS		
Fair value of plan assets at beginning of year	$32.7	31.1
Actual return on plan assets	2.6	3.0
Employer contributions	1.6	0.2
Plan participant contributions	--	--
Gross benefits paid	(1.8)	(1.6)
Fair value of plan assets at end of year	$35.1	32.7

Employer contributions and benefits paid under the pension plans include $0.2 million paid from employer assets in 2006 and 2005.

(Dollars in millions)	Pension Benefits 2006	2005
Funded Status		
Funded status at end of year	$(13.1)	(17.5)
Unrecognized prior service cost	0.1	--
Unrecognized net actuarial (gain) loss	10.1	13.3
Accrued benefit cost	(2.9)	(4.2)
Amounts recognized in the Balance Sheet consist of:		
Accrued benefit cost	(2.9)	(4.2)
Additional minimum liability	(10.3)	(13.3)
Intangible asset	0.1	--
Accumulated other comprehensive income (before tax effect)	10.2	13.3
Accrued benefit liability	$ (2.9)	(4.2)

A decrease of $3.0 million was included in other comprehensive income during 2006 arising from a change in the additional minimum liability.

The following table provides the components of net periodic benefit cost for the plans for the years ended September 30, 2006, 2005 and 2004:

(Dollars in millions)	Pension Benefits 2006	2005	2004
Service cost	$ --	--	0.6
Interest cost	2.6	2.6	2.5
Expected return on plan assets	(2.7)	(2.9)	(2.9)
Amortization of service costs	--	--	--
Net actuarial (gain) loss	0.4	0.2	0.1
Net amortization and deferral	--	--	--
Net periodic benefit cost	0.3	(0.1)	0.3
Defined contribution plans	2.9	2.4	1.9
Total	$3.2	2.3	2.2

The following weighted-average assumptions were used to determine the net periodic benefit cost for the pension plans:

	2006	2005	2004
Discount rate	5.25%	6.00%	6.00%
Rate of increase in compensation levels	N/A	N/A	4.00%
Expected long-term rate of return on assets	8.25%	8.25%	8.25%

The following weighted-average assumptions were used to determine the net periodic benefit obligations for the pension plans:

	2006	2005
Discount rate	5.75%	5.25%
Rate of increase in compensation levels	--	--

The assumed rate of increase in compensation levels is not applicable in 2005 and 2004 as the plan was frozen as of December 31, 2003.

The asset allocation for the Company's pension plans at the end of 2006 and 2005, the Company's acceptable range and the target allocation for 2007, by asset category, follows:

	Target Allocation	Acceptable Range	Percentage of Plan at Year-end	
ASSET CATEGORY	2007		2006	2005
Equity securities	60%	50-70%	66%	65%
Fixed income	40%	30-50%	32%	31%
Cash/cash equivalents	0%	0-5%	2%	4%

The Company's pension plan assets are managed by outside investment managers and assets are rebalanced when the target ranges are exceeded. Pension plan assets consist principally of marketable securities including common stocks, bonds, and interest-bearing deposits. The Company's investment strategy with respect to pension assets is to achieve a total rate of return (income and capital appreciation) that is sufficient to accomplish the purpose of providing retirement benefits to all eligible and future retirees of the pension plans. The Company regularly monitors performance and compliance with investment guidelines.

EXPECTED CASH FLOWS

Information about the expected cash flows for the pension and other postretirement benefit plans follows:

(Dollars in millions)	Pension Benefits	Other Benefits
Expected Employer Contributions -- 2007		$0.20.1
Expected Benefit Payments		
2007		2.20.1
2008		2.30.1
2009		2.30.1
2010		2.40.1
2011		2.50.1
2012-2016	$14.3	0.6

14. OTHER FINANCIAL DATA

Items charged to operations during the years ended September 30, 2006, 2005 and 2004 included the following:

(Dollars in thousands)	2006	2005	2004

Salaries and wages (including fringes)	$119,286	100,372	93,536
Maintenance and repairs	4,719	3,897	4,326
Research and development (R&D) costs:			

Company-sponsored	$ 20,043	16,829	12,201
Customer-sponsored	6,323	5,687	6,064
Total R&D	$ 26,366	22,516	18,265
Other engineering costs	9,069	7,763	9,636
Total R&D and other engineering costs	$ 35,435	30,279	27,901
As a % of net sales	7.7%	7.1%	6.6%

The increase in salaries and wages in 2006 compared to the prior years is mainly due to the current year acquisitions of Nexus and Hexagram and the addition of personnel at DCSI to support the near-term sales growth.

Customer-sponsored R&D is defined in note 1(O) of notes to consolidated financial statements.

A reconciliation of the changes in accrued product warranty liability for the years ended September 30, 2006, 2005, and 2004 is as follows:

	2006	2005	2004
Balance as of October 1	$ 1,487	2,147	1,374
Additions charged to expense	2,357	1,108	3,206
Deductions	(2,422)	(1,768)	(2,433)
Balance as of September 30	$ 1,422	1,487	2,147

15. BUSINESS SEGMENT INFORMATION

The Company is organized based on the products and services that it offers. Under this organizational structure, the Company has three reporting units: Communications, Filtration/Fluid Flow and RF Shielding and Test (Test). The Communications unit is a proven supplier of special purpose fixed network communications systems for electric, gas and water utilities, including hardware and software to support advanced metering applications. DCSI's Two-Way Automatic Communications System, known as TWACS(R), is currently used for automatic meter reading (AMR) and related advanced metering functions serving approximately 200 utilities, as well as having load management capabilities. Hexagram's STAR(R) system, the premier wireless Advanced Metering Infrastructure, delivers two-way and one-way operation on secure licensed radio frequencies for more than 100 utilities serving electric, gas and water customers. Nexus provides best-in-class information solutions to more than 85 leading energy companies that add value to existing billing and metering infrastructure to allow both the utilities and their customers to better manage energy-driven transactions and decision making. Comtrak's SecurVision(R) product line provides digital video surveillance and security functions for large commercial enterprises and alarm monitoring companies. Filtration/Fluid Flow primary operations consist of: PTI Technologies Inc. (PTI), VACCO Industries (VACCO) and Filtertek Inc. (Filtertek). PTI and VACCO develop and manufacture a wide range of filtration products and are leading suppliers of filters to the commercial and defense aerospace, satellite and industrial markets. Filtertek develops and manufactures a broad range of high-volume, original equipment manufacturer (OEM) filtration products at its facilities in North America, South America and Europe. Each of the components of the Filtration/Fluid Flow segment is presented separately due to differing long-term economics. Test segment operations represent the EMC Group, consisting primarily of EMC Test Systems, L.P. (ETS) and Lindgren RF Enclosures, Inc. (Lindgren). The EMC Group is principally involved in the design and manufacture of EMC test equipment, test chambers, and electromagnetic absorption materials. The EMC Group also manufactures radio frequency (RF) shielding products and components used by manufacturers of medical equipment, communications systems, electronic products, and shielded rooms for high security data processing and secure communication. Accounting policies of the segments are the same as those described in the summary of significant accounting policies in note 1 to the Consolidated Financial Statements.

In accordance with SFAS 131, the Company evaluates the performance of its operating units based on EBIT, which is defined as: Earnings Before Interest and Taxes. Intersegment sales and transfers are not significant. Segment assets consist primarily of customer receivables, inventories, capitalized software and fixed assets directly associated with the production processes of the segment. Segment depreciation and amortization is based upon the direct assets listed above.

NET SALES

(Dollars in millions)

Year ended September 30,	2006	2005	2004
Communications	$156.2	138.0	137.8
PTI	46.4	40.7	38.1
VACCO	32.3	38.9	43.2
Filtertek	95.4	92.1	92.6
Filtration/Fluid Flow subtotal	174.1	171.7	173.9
Test	128.6	119.4	110.4
Consolidated totals	$458.9	429.1	422.1

No customers exceeded 10% of net sales in the periods presented.

EBIT

(Dollars in millions)

Year ended September 30,	2006	2005	2004
Communications	$ 28.3	38.8	38.4
PTI	6.6	3.8	2.4
VACCO	6.1	10.4	13.7
Filtertek	6.8	8.2	5.7
Filtration/Fluid Flow subtotal	19.5	22.4	21.8
Test	15.0	12.2	11.3
Reconciliation to consolidated totals (Corporate)	(15.2)	(11.4)	(11.8)
Consolidated EBIT	47.6	62.0	59.7
Add: interest income	1.3	1.9	0.8
Earnings before income tax	$ 48.9	63.9	60.5

IDENTIFIABLE ASSETS

(Dollars in millions)

Year ended September 30,	2006	2005	2004
Communications	$ 97.9	52.4	51.3
PTI	32.0	36.7	39.7
VACCO	15.7	19.7	21.8
Filtertek	62.9	91.5	93.0
Filtration/Fluid Flow subtotal	110.6	147.9	154.5
Test	50.3	80.7	75.1
Reconciliation to consolidated totals (Corporate assets)	229.9	142.8	121.5
Consolidated totals	$488.7	423.8	402.4

Corporate assets consist primarily of goodwill, deferred taxes, acquired intangible assets and cash balances.

CAPITAL EXPENDITURES

(Dollars in millions)

Year ended September 30,	2006	2005	2004
Communications	$3.4	1.9	1.5
PTI	0.2	1.0	1.1
VACCO	1.0	0.7	0.6
Filtertek	3.8	4.0	6.7
Filtration/Fluid Flow subtotal	5.0	5.7	8.4
Test	0.7	1.2	0.9
Consolidated totals	$9.1	8.8	10.8

DEPRECIATION AND AMORTIZATION

(Dollars in millions)

Year ended September 30,	2006	2005	2004
Communications	$ 5.0	2.0	1.7
PTI	1.5	1.5	1.7
VACCO	0.7	0.7	0.7
Filtertek	6.0	6.2	6.0
Filtration/Fluid Flow subtotal	8.2	8.4	8.4
Test	1.3	1.4	1.4
Reconciliation to consolidated totals (Corporate)	2.8	0.4	0.4
Consolidated totals	$17.3	12.2	11.9

GEOGRAPHIC INFORMATION

NET SALES

(Dollars in millions)

Year ended September 30,	2006	2005	2004
United States	$355.9	325.3	330.6
Europe	40.2	56.0	58.3
Far East	36.1	29.6	18.8
Other	26.7	18.2	14.4
Consolidated totals	$458.9	429.1	422.1

LONG-LIVED ASSETS

(Dollars in millions)

Year ended September 30,	2006	2005	2004
United States	$51.3	50.3	53.5
Europe	10.6	10.9	11.6
Other	6.9	6.0	4.0
Consolidated totals	$68.8	67.2	69.1

Net sales are attributed to countries based on location of customer. Long-lived assets are attributed to countries based on location of the asset.

16. COMMITMENTS AND CONTINGENCIES

At September 30, 2006, the Company had $1.5 million in letters of credit outstanding as guarantees of contract performance. As a normal incidence of the businesses in which the Company is engaged, various claims, charges and litigation are asserted or commenced against the Company. Lindgren is involved in a contract dispute with a prime contractor involving the assertion of certain construction delay damages of approximately $3.7 million. The project was completed in 2005. Lindgren vigorously denies responsibility for this delay and for these damages, and has asserted a claim against the prime contractor of $0.9 million based on damages suffered by Lindgren. Lindgren continues to aggressively defend its position and pursue its right to affirmative damages however, there can be no assurance of the outcome at this time. With respect to claims and litigation asserted or commenced against the Company, it is the opinion of Management, that final judgments, if any, which might be rendered against the Company are adequately reserved, covered by insurance, or are not likely to have a material adverse effect on its financial condition or results of operation.

17. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

(Dollars in thousands, except per share amounts)	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER	FISCAL YEAR
2006					
Net sales	$ 90,586	122,884	123,626	121,769	458,865
Net earnings	2,204	7,343	11,163	10,570	31,280
Basic earnings per share:					
Net earnings	.09	.29	.43	.41	1.22
Diluted earnings per share:					
Net earnings	$ .08	.28	.42	.40	1.19
2005					
Net sales	$104,375	106,160	108,800	109,780	429,115
Net earnings	10,523	10,427	12,401	10,193	43,544
Basic earnings per share:					
Net earnings	.41	.41	.49	.40	1.71
Diluted earnings per share:					
Net earnings	$ .40	.40	.47	.39	1.66

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Company's Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in the Securities Exchange Act Rule 13a-15(f)). Our internal control over financial reporting is 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 in the United States of America.

Because of its inherent limitations, any system of internal control over financial reporting, no matter how well designed, may not prevent or detect misstatements due to the possibility that a control can be circumvented or overridden or that misstatements due to error or fraud may occur that are not detected. Also, because of changes in conditions, internal control effectiveness may vary over time.

Management assessed the effectiveness of the Company's internal control over financial reporting as of September 30, 2006 using criteria established in Internal Control -- Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and concluded that the Company maintained effective internal control over financial reporting as of September 30, 2006 based on these criteria, subject to the scope limitation with respect to Nexus and Hexagram as discussed in the following paragraph.

The Company acquired Nexus Energy Software, Inc. (Nexus) on November 29, 2005 and Hexagram, Inc. (Hexagram) on February 1, 2006. As permitted by SEC guidance, Management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of September 30, 2006, Nexus' and Hexagram's internal control over financial reporting. Total assets related to Nexus as of September 30, 2006 were $3.7 million and revenues for the ten-month period subsequent to the acquisition (November 29, 2005 to September 30, 2006) were $9.6 million. Total assets related to Hexagram as of September 30, 2006 were $13.1 million and revenues for the eight-month period subsequent to the acquisition (February 1, 2006 to September 30, 2006) were $18.6 million.

Our internal control over financial reporting as of September 30, 2006, as well as our assessment of the effectiveness of our internal control over financial reporting as of September 30, 2006, have been audited by KPMG LLP, an independent registered public accounting firm, as stated in the report which is included herein.

Victor L. Richey Chairman, Chief Executive Officer, and President	Gary E. Muenster Senior Vice President and Chief Financial Officer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
ESCO Technologies Inc.:

We have audited the accompanying consolidated balance sheets of ESCO Technologies Inc. and subsidiaries (the Company) as of September 30, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements 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 consolidated financial statements referred to previously present fairly, in all material respects, the financial position of ESCO Technologies Inc. and subsidiaries as of September 30, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended September 30, 2006, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment" effective October 1, 2005 and the Company changed its method of quantifying errors in 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of ESCO Technologies Inc.'s internal control over financial reporting as of September 30, 2006, based on criteria established in the Internal Control -- Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated December 11, 2006, expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

St. Louis, Missouri
December 11, 2006

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
ESCO Technologies Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that ESCO Technologies Inc. (the Company) maintained effective internal control over the financial reporting as of September 30, 2006, based on criteria established in the Internal Control -- Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). ESCO Technologies 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. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of 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 required 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, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, 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 the 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, management's assessment that ESCO Technologies Inc. maintained effective internal control over financial reporting as of September 30, 2006, is fairly stated, in all material respects, based on criteria established in the Internal Control -- Integrated Framework issued by COSO. Also, in our opinion, ESCO Technologies Inc. maintained, in all material respects, effective internal control over financial reporting as of September 30, 2006, based on criteria established in the Internal Control -- Integrated Framework issued by COSO.

The Company acquired Nexus Energy Software, Inc. (Nexus) on November 29, 2005 and Hexagram, Inc. (Hexagram) on February 1, 2006, and management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of September 30, 2006, Nexus' and Hexagram's internal control over financial reporting. Total assets related to Nexus as of September 30, 2006 of $3.7 million and revenues for the ten-month period subsequent to the acquisition (November 29, 2005 to September 30, 2006) of $9.6 million and total assets related to Hexagram as of September 30, 2006 of $13.1 million and revenues for the eight-month period subsequent to the acquisition (February 1, 2006 to September 30, 2006) of $18.6 million were included in the consolidated financial statements of ESCO Technologies Inc. and subsidiaries as of and for the year ended September 30, 2006. Our audit of internal control over financial reporting of ESCO Technologies Inc. also excluded an evaluation of the internal control over financial reporting of Nexus and Hexagram.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of ESCO Technologies Inc. and subsidiaries as of September 30, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the years in the three-year period ended September 30, 2006, and our report dated December 11, 2006, expressed an unqualified opinion on those consolidated financial statements.

St. Louis, Missouri
December 11, 2006

FIVE-YEAR FINANCIAL SUMMARY

(Dollars in millions, except per share amounts)	2006	2005	2004	2003	2002
For years ended September 30:					
Net sales	$458.9	429.1	422.1	396.7	316.6
Net earnings from continuing operations	31.3	43.5	37.8	26.7	23.3
Net earnings (loss) from discontinued operations	--	--	(2.1)	(66.5)	(1.6)
Net earnings (loss) before accounting change	31.3	43.5	35.7	(39.7)	21.8
Net earnings (loss)	31.3	43.5	35.7	(41.1)	21.8
Earnings (loss) per share:					
Basic:					
Continuing operations	1.22	1.71	1.47	1.05	0.93
Discontinued operations	--	--	(0.09)	(2.62)	(0.06)
Cumulative effect of accounting change, net of tax	--	--	--	(0.06)	--
Net earnings (loss)	1.22	1.71	1.38	(1.63)	0.87
Diluted:					
Continuing operations	1.19	1.66	1.42	1.02	0.90
Discontinued operations	--	--	(0.08)	(2.53)	(0.06)
Cumulative effect of accounting change, net of tax	--	--	--	(0.06)	--
Net earnings (loss)	1.19	1.66	1.34	(1.57)	0.84
As of September 30:					
Working capital	131.4	197.2	165.2	120.5	112.6
Total assets	488.7	423.8	402.4	393.4	407.7
Long-term debt	--	--	0.4	0.5	0.5
Shareholders' equity	$376.4	331.0	307.6	275.4	306.3

See notes 2 and 3 of notes to consolidated financial statements for discussion of acquisition and divestiture activity.

COMMON STOCK MARKET PRICE

ESCO's common stock and associated preferred stock purchase rights (subsequently referred to as common stock) are listed on the New York Stock Exchange under the symbol "ESE." The following table summarizes the high and low prices of the common stock for each quarter of fiscal 2006 and 2005. The prior year amounts have been adjusted to reflect the 2-for-1 stock split which occurred on September 23, 2005.

	2006		2005	
Quarter	HIGH	LOW	High	Low
First	$50.75	32.57	$39.48	32.25
Second	52.76	43.84	42.43	34.49
Third	58.03	47.65	53.25	35.40
Fourth	58.42	45.30	56.23	47.18

ESCO historically has not paid cash dividends on its common stock. Management continues to evaluate its cash dividend policy. There are no current plans to initiate a dividend.

SHAREHOLDERS' SUMMARY

SHAREHOLDERS' ANNUAL MEETING

The Annual Meeting of the shareholders of ESCO Technologies Inc. will be held at 9:30 a.m. Friday, February 2, 2007, at the Company's Corporate headquarters, 9900A Clayton Road, St. Louis, Missouri 63124. Notice of the meeting and a proxy statement were sent to shareholders with this Annual Report.

CERTIFICATIONS

Pursuant to New York Stock Exchange (NYSE) requirements, the Company submitted to the NYSE the annual certifications, dated February 27, 2006 and March 3, 2005, by the Company's chief executive officer that he was not aware of any violations by the Company of NYSE's corporate governance listing standards. In addition, the Company filed with the Securities and Exchange Commission the certifications by the Company's chief executive officer and chief financial officer required under Section 302 of the Sarbanes-Oxley Act of 2002 as exhibits to the Company's Forms 10-K for its fiscal years ended September 30, 2006 and September 30, 2005.

10-K REPORT

A copy of the Company's 2006 Annual Report on Form 10-K filed with the Securities and Exchange Commission is available to shareholders without charge. Direct your written request to the Investor Relations Department, ESCO Technologies Inc., 9900A Clayton Road, St. Louis, Missouri 63124. The Form 10-K is also available on the Company's web site at www.escotechnologies.com.

INVESTOR RELATIONS

Additional investor-related information may be obtained by contacting the Director of Investor Relations at (314) 213-7277 or toll free at (888) 622-3726. Information is also available through the Company's web site at www.escotechnologies.com or via e-mail to pmoore@escotechnologies.com.

TRANSFER AGENT AND REGISTRAR

Shareholder inquiries concerning lost certificates, transfer of shares or address changes should be directed to:

Registrar and Transfer Company
10 Commerce Drive
Cranford, NJ 07016-3572
1 (800) 368-5948
E-mail: info@rtco.com

CAPITAL STOCK INFORMATION

ESCO Technologies Inc. common stock shares (symbol ESE) are listed on the New York Stock Exchange. There were approximately 2,500 holders of record of shares of common stock at September 30, 2006.

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

KPMG LLP
10 South Broadway, Suite 900
St. Louis, Missouri 63102

EXHIBIT 21

SUBSIDIARIES OF
ESCO TECHNOLOGIES INC.

NAME	STATE OR JURISDICTION OF INCORPORATION OR ORGANIZATION	NAME UNDER WHICH IT DOES BUSINESS
Beijing Lindgren ElectronMagnetic Technology Co., Ltd.	People's Republic of China	Same
Comtrak Technologies, L.L.C.	Missouri	Same
Distribution Control Systems Caribe, Inc.	Puerto Rico	Same
Distribution Control Systems, Inc.	Missouri	Same
ETS-Lindgren, L.P.	Texas	Same and Acoustics Systems
ETS-Lindgren Japan, Inc.	Japan	Same
ESCO Electronica De Mexico, S.A. de C.V.	Mexico	Same
ESCO Technologies Holding Inc.	Delaware	Same
Euroshield OY	Finland	Same
Filtertek Inc. (including its Tek Packaging Division)	Delaware	Same
Filtertek BV	Netherlands	Same
Filtertek do Brasil Industria E	Brazil	Same
Commercio LTDA Filtertek SA	France	Same
Hexagram, Inc.	Ohio	Same
Lindgren R.F. Enclosures, Inc.	Illinois	Same and ETS-Lindgren
Nexus Energy Software, Inc.	Massachusetts	Same
PTI Technologies Inc.	Delaware	Same
Ray Proof Limited	England	Same
VACCO Industries	California	Same

EXHIBIT 23

Consent of Independent Registered Public Accounting Firm

The Board of Directors
ESCO Technologies Inc.:

We consent to the incorporation by reference in the registration statements (Nos. 33-39737, 33-47916, 33-98112, 333-92945, 333-77887, 333-96309, 333-63930, 333-85268, and 333-117953) on Form S-8 of ESCO Technologies Inc. (the Company) of our reports dated December 11, 2006, with respect to the consolidated balance sheets of ESCO Technologies Inc. and subsidiaries as of September 30, 2006 and 2005 and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2006; management's assessment of the effectiveness of internal control over financial reporting as of September 30, 2006 and the effectiveness of internal control over financial reporting as of September 30, 2006, which reports appear in the Annual Report to Stockholders for the fiscal year ended September 30, 2006 and is incorporated by reference in the September 30, 2006 annual report on Form 10-K of the Company.

Our report dated December 11, 2006 on the consolidated financial statements refers to the adoption of Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment" and change in the method of quantifying errors.

The Company acquired Nexus Energy Software, Inc. (Nexus) on November 29, 2005 and Hexagram, Inc. (Hexagram) on February 1, 2006, and management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of September 30, 2006, Nexus' and Hexagram's internal control over financial reporting. Total assets related to Nexus as of September 30, 2006 of $3.7 million and revenues for the ten-month period subsequent to the acquisition (November 29, 2005 to September 30, 2006) of $9.6 million and total assets related to Hexagram as of September 30, 2006 of $13.1 million and revenues for the eight-month period subsequent to the acquisition (February 1, 2006 to September 30, 2006) of $18.6 million were included in the consolidated financial statements of the Company as of and for the year ended September 30, 2006. Our audit of internal control over financial reporting of the Company also excluded an evaluation of the internal control over financial reporting of Nexus and Hexagram.

/s/ KPMG LLP

St. Louis, Missouri
December 11, 2006

EXHIBIT 31.1

CERTIFICATION

I, V.L. Richey, Jr., certify that:

1. I have reviewed this annual report on Form 10-K of ESCO Technologies 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 and finance 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: December 11, 2006

/s/ V.L. Richey, Jr.
V.L. Richey, Jr.
Chairman, President and
Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION

I, G.E. Muenster, certify that:

1. I have reviewed this annual report on Form 10-K of ESCO Technologies 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 and finance 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: December 11, 2006

/s/ G.E. Muenster

G.E. Muenster
Sr. Vice President and 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

In connection with the annual report of ESCO Technologies Inc. (the "Company") on Form 10-K for the period ended September 30, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, V. L. Richey, Jr., Chairman and Chief Executive Officer of the Company, and G. E. Muenster, Vice President and Chief Financial Officer of the Company, certify, to the best of our knowledge, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: December 13, 2006

/s/ V.L. Richey, Jr.
V.L. Richey, Jr.
Chairman, President and Chief Executive Officer

/s/ G.E. Muenster
G.E. Muenster
Sr. Vice President and Chief Financial Officer