

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORP

Form 10-Q

August 07, 2006

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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FORM 10-Q

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☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended June 30, 2006

OR

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

Commission file number: 1-13782

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**25-1615902**  
(I.R.S. Employer  
Identification No.)

**1001 Air Brake Avenue**

**Wilmerding, PA**  
(Address of principal executive offices)

**15148**  
(Zip Code)

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**412-825-1000**

(Registrant's telephone number, including area code)

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N/A

(Former name, former address and former fiscal year, if changed since last report)

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

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 ☐ Non-accelerated filer ☐

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

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

Class	Outstanding at August 2, 2006
[Common Stock, \$.01 par value per share]	48,772,584 shares

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**WESTINGHOUSE AIR BRAKE  
TECHNOLOGIES CORPORATION**

**June 30, 2006 FORM 10-Q**

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**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS**

<i>In thousands, except shares and par value</i>		<b>Unaudited June 30, 2006</b>	<b>December 31, 2005</b>
<b>Assets</b>			
<b>Current Assets</b>			
Cash and cash equivalents		\$ 238,907	\$ 141,365
Accounts receivable		162,993	206,891
Inventories		139,737	110,873
Deferred income taxes		15,612	15,838
Other current assets		12,444	7,959
Total current assets		569,693	482,926
Property, plant and equipment		372,344	358,759
Accumulated depreciation		(207,848)	(197,158)
Property, plant and equipment, net		164,496	161,601
<b>Other Assets</b>			
Goodwill		119,270	118,181
Other intangibles, net		38,100	39,129
Deferred income taxes		18,526	18,428
Other noncurrent assets		10,364	16,092
Total other assets		185,260	191,830
Total Assets		\$ 920,449	\$ 836,357
<b>Liabilities and Shareholders' Equity</b>			
<b>Current Liabilities</b>			
Accounts payable		\$ 80,555	\$ 93,551
Accrued income taxes		11,557	4,427
Customer deposits		93,750	71,098
Accrued compensation		23,272	25,274
Accrued warranty		17,557	16,158
Other accrued liabilities		28,754	30,971
Total current liabilities		255,445	241,479
Long-term debt		150,000	150,000
Reserve for postretirement and pension benefits		43,347	44,428
Deferred income taxes		7,582	7,381
Other long-term liabilities		10,230	13,862
Total liabilities		466,604	457,150
<b>Shareholders' Equity</b>			
Preferred stock, 1,000,000 shares authorized, no shares issued			

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Common stock, \$.01 par value; 100,000,000 shares authorized: 66,174,767 shares issued and 48,659,930 and 48,002,819 outstanding at June 30, 2006 and December 31, 2005, respectively.	662	662
Additional paid-in capital	309,944	294,209
Treasury stock, at cost, 17,514,837 and 18,171,948 shares, at June 30, 2006 and December 31, 2005, respectively	(217,253)	(225,483)
Retained earnings	376,974	336,744
Accumulated other comprehensive loss	(16,482)	(26,925)
Total shareholders' equity	453,845	379,207
Total Liabilities and Shareholders' Equity	\$ 920,449	\$ 836,357

The accompanying notes are an integral part of these statements.

**Table of Contents****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

<i>In thousands, except per share data</i>	<b>Unaudited</b>		<b>Unaudited</b>	
	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30</b>		<b>June 30</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net sales	\$ 261,902	\$ 266,297	\$ 524,311	\$ 508,097
Cost of sales	(185,161)	(200,122)	(372,480)	(384,910)
Gross profit	76,741	66,175	151,831	123,187
Selling, general and administrative expenses	(32,313)	(30,623)	(65,941)	(59,635)
Engineering expenses	(8,023)	(8,183)	(16,138)	(16,853)
Amortization expense	(859)	(1,073)	(1,726)	(2,044)
Total operating expenses	(41,195)	(39,879)	(83,805)	(78,532)
Income from operations	35,546	26,296	68,026	44,655
Other income and expenses				
Interest expense, net	(420)	(2,165)	(1,544)	(4,649)
Other expense, net	(1,623)	(687)	(1,503)	(1,836)
Income from continuing operations before income taxes	33,503	23,444	64,979	38,170
Income tax expense	(11,721)	(8,511)	(23,129)	(13,894)
Income from continuing operations	21,782	14,933	41,850	24,276
Discontinued operations				
(Loss) income from discontinued operations (net of tax)	(637)	218	(659)	123
Net income	\$ 21,145	\$ 15,151	\$ 41,191	\$ 24,399
<b>Earnings Per Common Share</b>				
<b>Basic</b>				
Income from continuing operations	\$ 0.45	\$ 0.32	\$ 0.87	\$ 0.52
(Loss) income from discontinued operations	(0.01)		(0.02)	0.01
Net income	\$ 0.44	\$ 0.32	\$ 0.85	\$ 0.53
<b>Diluted</b>				
Income from continuing operations	\$ 0.44	\$ 0.31	\$ 0.86	\$ 0.51
(Loss) income from discontinued operations	(0.01)	0.01	(0.02)	.01
Net income	\$ 0.43	\$ 0.32	\$ 0.84	\$ 0.52
<b>Weighted average shares outstanding</b>				
Basic	48,451	46,862	48,210	46,452
Diluted	49,092	47,544	48,851	47,157

The accompanying notes are an integral part of these statements.



**Table of Contents****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Unaudited</b>	
	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>
<i>In thousands</i>		<b>Revised</b>
<b>Operating Activities</b>		
Net income	\$ 41,191	\$ 24,399
Stock-based compensation expense	5,981	625
Adjustments to reconcile net income to net cash provided by operations:		
Discontinued operations	(1,154)	(20)
Depreciation and amortization	11,859	13,352
Excess income tax benefits from exercise of stock options	(4,215)	
Changes in operating assets and liabilities		
Accounts receivable	39,876	(18,812)
Inventories	(30,989)	(14,842)
Accounts payable	(12,755)	14,276
Accrued income taxes	22,279	10,189
Accrued liabilities and customer deposits	(10,977)	1,559
Other assets and liabilities	12,401	(437)
Net cash provided by operating activities	73,497	30,289
<b>Investing Activities</b>		
Purchase of property, plant and equipment	(8,969)	(11,452)
Disposals of property, plant and equipment		975
Acquisition of business, net of cash received		(36,405)
Sale of discontinued operations	3,018	
Discontinued operations		(2)
Net cash used for investing activities	(5,951)	(46,884)
<b>Financing Activities</b>		
Repayments of long term debt		(107)
Proceeds from the issuance of treasury stock for stock options and other benefit plans	9,895	16,500
Excess income tax benefits from exercise of stock options	4,215	
Cash dividends (\$0.02 per share for the six months ended June 30, 2006 and 2005)	(969)	(932)
Net cash provided by financing activities	13,141	15,461
Effect of changes in currency exchange rates	16,855	(7,271)
(Decrease) increase in cash	97,542	(8,405)
Cash, beginning of year	141,365	95,257
Cash, end of period	\$ 238,907	\$ 86,852

The accompanying notes are an integral part of these statements.



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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

**1. BUSINESS**

Wabtec is one of the world's largest providers of value-added, technology-based products and services for the global rail industry. Our products are found on virtually all U.S. locomotives, freight cars and passenger transit vehicles, as well as in more than 80 countries throughout the world. Our products enhance safety, improve productivity and reduce maintenance costs for customers, and many of our core products and services are essential in the safe and efficient operation of freight rail and passenger transit vehicles. Wabtec is a global company with operations in 11 countries. In the first six months of 2006, about 32 percent of the Company's revenues came from outside the U.S.

**2. ACCOUNTING POLICIES**

**Basis of Presentation** The unaudited condensed consolidated interim financial statements have been prepared in accordance with generally accepted accounting principles and the rules and regulations of the Securities and Exchange Commission and include the accounts of Wabtec and its majority owned subsidiaries. These condensed interim financial statements do not include all of the information and footnotes required for complete financial statements. In management's opinion, these financial statements reflect all adjustments of a normal, recurring nature necessary for a fair presentation of the results for the interim periods presented. Results for these interim periods are not necessarily indicative of results to be expected for the full year.

The Company operates on a four-four-five week accounting quarter, and accordingly, the quarters end on or about March 31, June 30, September 30 and December 31.

The notes included herein should be read in conjunction with the audited consolidated financial statements included in Wabtec's Annual Report on Form 10-K for the year ended December 31, 2005. The December 31, 2005 information has been derived from the Company's December 31, 2005 Annual Report on Form 10-K.

**Revenue Recognition** Revenue is recognized in accordance with Staff Accounting Bulletins (SABs) 101, "Revenue Recognition in Financial Statements" and 104, "Revision of Topic 13". Revenue is recognized when products have been shipped to the respective customers, title has passed and the price for the product has been determined.

The Company recognizes revenues on long-term contracts based on the percentage of completion method of accounting. The units-of-delivery method or other measures, as appropriate, are used to measure the progress toward completion of individual contracts. Contract revenues and cost estimates are reviewed and revised at a minimum quarterly and adjustments are reflected in the accounting period as such amounts are determined. Provisions are made currently for estimated losses on uncompleted contracts.

Certain pre-production costs relating to long-term production and supply contracts have been deferred and will be recognized over the life of the contracts. Deferred pre-production costs were \$6.9 million and \$4.9 million at June 30, 2006 and December 31, 2005, respectively.

**Use of Estimates** The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from the estimates. On an ongoing basis, management reviews its estimates based on currently available information. Changes in facts and circumstances may result in revised estimates.

**Table of Contents****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

**Stock-Based Compensation** Effective January 1, 2006, Wabtec adopted Statement of Financial Accounting Standards ( SFAS ) No. 123 (revised 2004), Share-Based Payment, which requires the company to recognize compensation expense for stock-based compensation based on the grant date fair value. This expense must be recognized ratably over the requisite service period following the date of grant. Wabtec has elected the modified prospective transition method for adoption, and prior periods financial statements have not been restated. Prior to January 1, 2006, Wabtec accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees, and related interpretations.

*Pro Forma Effect Prior to the Adoption of SFAS No. 123(R)* Wabtec's net income and earnings per share for 2005 would have been reduced to the pro forma amounts shown below if compensation expense had been determined based on the fair value at the grant dates in accordance with SFAS No. 123, Accounting for Stock-Based Compensation, and SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure an amendment of FASB Statement No. 123.

<i>In thousands, except per share</i>	<b>Three months ended June 30, 2005</b>	<b>Six months ended June 30, 2005</b>
Net income as reported	\$ 15,151	\$ 24,399
Stock based compensation expense under FAS123, net of tax of \$162 and \$348	283	604
Pro forma	\$ 14,868	\$ 23,795
Basic earnings per share		
As reported	\$ 0.32	\$ 0.53
Pro forma	0.32	0.51
Diluted earnings per share		
As reported	\$ 0.32	\$ 0.52
Pro forma	0.31	0.50

**Stock-Based Plans** Stock options have been granted at not less than market prices on the dates of grant. Generally, the options become exercisable over a three-year vesting period and expire ten years from the date of grant. In January 2006, Wabtec granted 32,000 stock options to certain individuals. The Company has now adopted a non-vested stock plan and issued 200,500 awards to executives in February 2006. The non-vested stock generally vests over four years from the date of grant. In addition, the Company established in 2004, a stock-based incentive plan for eligible employees. The plan provides stock awards which vest upon attainment of certain three year performance targets. Wabtec also sponsors an employee stock purchase plan, whereby participants can purchase the Company's common stock at a discount of about 15% of the lesser of fair market value on the first or last day of each offering period.

Stock based compensation was \$6.0 million and \$625,000 for the six months ended June 30, 2006 and 2005, respectively. This included \$5 million and \$625,000, respectively, related to non-vested stock and the stock awards under the incentive plan, the accounting for which was not impacted significantly by the adoption of SFAS No. 123(R). As a result of adopting SFAS No. 123(R), compensation expense increased by \$291,000 and \$670,000 for the three and six month periods ended June 30, 2006, respectively, and basic and diluted earnings per share decreased by about \$0.01 and \$0.01, respectively. At June 30, 2006, unamortized compensation expense related to those stock options, non-vested shares and stock awards expected to vest totaled \$15.3 million and will be recognized over a weighted average period of 1.8 years.

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Wabtec uses a Black-Scholes pricing model to estimate fair value at grant date for future option grants. 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:

	<b>Three and six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>
Dividend yield	.3%	.3%
Risk-free interest rate	4.27%	4.6%
Stock price volatility	43.4	44.3
Expected life (years)	5.0	5.0

The dividend yield is based on the Company's dividend rate and the current market price of the underlying common stock at the date of grant. Expected life in years is determined from historical stock option exercise data. Expected volatility is based on the historical volatility of Wabtec stock. The risk-free interest rate is based on the U.S. Treasury bond rates for the expected life of the option.

The following table summarizes the stock option activity and related information for the period indicated:

		<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Life</b>	<b>Aggregate intrinsic value (in thousands)</b>
<b>Options</b>				
Beginning of year January 1, 2006	2,204,065	\$ 13.98		\$ 28,477
Granted	32,000	26.66		344
Exercised	(610,887)	14.37		12,071
Canceled				
 Year to date June 30, 2006	 1,625,178	 \$ 14.08	 5.8	 \$ 37,896
 Exercisable	 1,346,156	 \$ 13.23	 5.3	 \$ 32,535
 Weighted average fair value of options granted during 2006	 \$ 11.19			

The following table summarizes the non-vested stock and stock awards activity and related information for the period indicated:

	<b>Non-Vested Stock</b>	<b>Stock Awards</b>	<b>Weighted Average FMV</b>
Outstanding at January 1, 2006		518,666	\$ 15.83
Granted	200,500	187,000	34.06
Canceled		(4,000)	16.11

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Outstanding at June 30, 2006	200,500	701,666	\$	27.75
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As of June 30, 2006, stock awards issued under the incentive plan are awarded but not vested. These stock awards will vest based upon the achievement of certain financial goals for each three year periods ending December 31, 2006, 2007 and 2008, respectively. The stock awards included in the table above represent the maximum number of shares that may ultimately vest. As of June 30, 2006, based on the Company's performance, we estimate that the majority of these stock awards will vest and have recorded compensation expense

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accordingly. If our estimate of the number of these stock awards expected to vest changes in a future accounting period, compensation expense could be reduced and will be recognized over the remaining vesting period.

**Financial Derivatives and Hedging Activities** The Company has entered into foreign currency forward contracts to reduce the impact of changes in currency exchange rates. Forward contracts are agreements with counterparty to exchange two distinct currencies at a set exchange rate for delivery on a set date at some point in the future. There is no exchange of funds until the delivery date. At the delivery date the Company can either take delivery of the currency or settle on a net basis. All outstanding forward contracts are for the sale of U.S. Dollars (USD) and the purchase of Canadian Dollars (CAD). As of June 30, 2006, the Company had forward contracts with a notional value of \$30.0 million CAD (or \$25.2 million U.S.), with an average exchange rate of \$.84 USD per \$1 CAD, resulting in the recording of a current asset and an increase in comprehensive income of \$1.1 million, net of tax.

**Foreign Currency Translation** Assets and liabilities of foreign subsidiaries, except for the Company's Mexican operations whose functional currency is the U.S. Dollar, are translated at the rate of exchange in effect on the balance sheet date while income and expenses are translated at the average rates of exchange prevailing during the year. Foreign currency gains and losses resulting from transactions, and the translation of financial statements are recorded in the Company's consolidated financial statements based upon the provisions of SFAS No. 52, Foreign Currency Translation. The effects of currency exchange rate changes on intercompany transactions and balances of a long-term investment nature are accumulated and carried as a component of shareholders' equity. The effects of currency exchange rate changes on intercompany transactions that are non U.S. dollar denominated amounts are charged or credited to earnings. Foreign exchange loss was \$1.3 million and \$637,000 for the three months ended June 30, 2006 and 2005, respectively, and \$930,000 and \$1.6 million for the six months ended June 30, 2006 and 2005, respectively.

**Other Comprehensive Income (Loss)** Comprehensive income (loss) is defined as net income and all other non-owner changes in shareholders' equity. The Company's accumulated other comprehensive income (loss) consists of foreign currency translation adjustments, foreign currency hedges and pension related adjustments. Six month changes in the table below, adjust components of accumulated other comprehensive income (loss). Total comprehensive income was:

<i>In thousands</i>	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net income	\$ 21,145	\$ 15,151	\$ 41,191	\$ 24,399
Foreign currency translation adjustment	9,928	(5,203)	10,220	(7,281)
Unrealized loss on foreign exchange contracts, net of tax	492	(1,303)	224	(2,092)
Total comprehensive income	\$ 31,565	\$ 8,645	\$ 51,635	\$ 15,026

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

As reflected on the balance sheet as a component of equity, components of accumulated other comprehensive income (loss) consisted of the following:

<i>In thousands</i>	<b>June 30, 2006</b>	<b>December 31, 2005</b>
Foreign currency translation adjustment	\$ 8,744	\$ (1,476)
Unrealized gains on foreign exchange contracts, net of tax	1,100	877
Additional minimum pension liability, net of tax	(26,326)	(26,326)
 Total accumulated comprehensive loss	 \$ (16,482)	 \$ (26,925)

**Reclassifications** Certain prior year amounts have been reclassified where necessary, to conform to the current year presentation.

**Recent Accounting Pronouncements** In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109. FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that it has taken or expects to take on a tax return. FIN 48 is effective in the first quarter of 2007. Wabtec is currently evaluating the impact of this statement on the company.

### 3. ACQUISITIONS AND DISCONTINUED OPERATIONS

On February 1, 2005, the Company completed the acquisition of the assets of Rütgers Rail S.p.A, a business with operations in Italy, Germany, France and Spain. The acquisition was accounted for as a purchase and accordingly, the purchase price was allocated to the respective assets and liabilities based upon their estimated fair values as of the acquisition date. Operating results were included in the consolidated statement of operations from the acquisition date forward. The new company formed to hold the newly purchased assets of Rütgers Rail S.p.A. is named CoFren S.r.l. ( CoFren ). CoFren is one of the leading manufacturers of brake shoes, disc pads and interior trim components for rail applications in Europe. The purchase price was \$35.9 million, net of cash received, resulting in additional goodwill of \$5.7 million.

For pro forma purposes, this acquisition would only impact the results for the six months ended June 30, 2005, as CoFren was included in its entirety for all periods beginning afterwards. The following unaudited pro forma financial information presents income statement results as if the acquisition had occurred January 1, 2005:

<i>In thousands, except per share</i>	<b>Six months ended June 30, 2005</b>
Net sales	\$ 513,833
Gross profit	124,752
Net income	24,509
Diluted earnings per share	
As reported	\$ 0.53
Pro forma	0.52

With the acquisition of Rutgers Rail, S.p.A., the Company decided to offer for sale a non-core product division. As part of the purchase accounting, the net amount of this division had been revalued to its estimated net realizable value and had been classified as assets held for sale, which is included in other noncurrent assets on the balance sheet.



**Table of Contents****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

At March 31, 2006, the sale of this division was completed for approximately \$2.0 million in cash, subject to a working capital adjustment which is expected to be finalized with the buyer in the 3rd quarter. The assets sold primarily included transit car interior products and services for customers located in Europe. This sale resulted in a loss of approximately \$740,000 subject to the working capital adjustment mentioned earlier. Also, in the fourth quarter of 2005, the Company decided to liquidate its bus door joint venture in China.

In accordance with SFAS 144, *Accounting for Impairment or Disposal of Long-Lived Assets*, the operating results of these businesses have been classified as discontinued operations for all years presented and are summarized as of December 31, as follows:

<i>In thousands</i>	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net sales	\$ 3	\$ 3,251	\$ 2,600	\$ 6,335
Income/(loss) before income taxes	(522)	377	(497)	253
Income tax expense	115	159	162	130
Loss from discontinued operations	\$ (637)	\$ 218	\$ (659)	\$ 123

**4. INVENTORIES**

The components of inventory, net of reserves, were:

<i>In thousands</i>	<b>June 30, 2006</b>	<b>December 31, 2005</b>
Raw materials	\$ 42,751	\$ 38,724
Work-in-process	74,716	54,953
Finished goods	22,270	17,196
Total inventory	\$ 139,737	\$ 110,873

**5. RESTRUCTURING AND IMPAIRMENT CHARGES**

In the first six months of 2005, the Company recorded restructuring and asset impairment charges totaling \$2.3 million related to consolidating two U.K. facilities into one, relocating a product line from Canada to the U.S., and completion of a data center migration. These charges consisted of severance costs of \$593,000 for 43 employees, relocation and other costs of \$469,000 and asset write-offs of \$1.2 million. All but \$475,000 of these costs were paid for in the first six months of 2005.

In the fourth quarter of 2005, the Company recorded restructuring charges related to consolidating facilities of about \$800,000. As of June 30, 2006, these costs have not been paid.

On July 19, 2006, the Board of Directors approved a restructuring plan to improve the profitability and efficiency of certain business units. As part of the plan, Wabtec will downsize two of its Canadian plants, in Stoney Creek and Wallaceburg, by moving certain products to lower-cost facilities and outsourcing. The restructuring plan will result in the recognition of \$11 million of expenses, pre-tax, primarily for pension-related curtailment and settlement charges and fixed asset write downs for idled assets. These expenses will be recognized in the second half of 2006.



and the first half of 2007.

#### **6. INTANGIBLES**

Goodwill on the balance sheet is \$119.3 million at June 30, 2006 and \$118.2 million at December 31, 2005.

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As of June 30, 2006 and December 31, 2005, the Company's trademarks had a net carrying amount of \$20.0 million and \$19.9 million, respectively, and the Company believes these intangibles have an indefinite life. Intangible assets of the Company, other than goodwill and trademarks, consist of the following:

<i>In thousands</i>	<b>June 30, 2006</b>	<b>December 31, 2005</b>
Patents and other, net of accumulated amortization of \$26,232 and \$22,459	\$ 8,503	\$ 9,987
Customer relationships, net of accumulated amortization of \$242 and \$145	3,170	3,018
Covenants not to compete, net of accumulated amortization of \$8,324 and \$8,304		20
Intangible pension asset	6,457	6,457
<b>Total</b>	<b>\$ 18,130</b>	<b>\$ 19,182</b>

The weighted average useful life of patents was 13 years, customer relationships were 20 years and covenants not to compete was five years. Amortization expense for intangible assets was \$675,000 and \$1.4 million for the three and six months ended June 30, 2006, and \$859,000 and \$1.6 million for the three and six months ended June 30, 2005.

The change in the carrying amount of goodwill by segment for the six months ended June 30, 2006 is as follows:

<i>In thousands</i>	<b>Freight Group</b>	<b>Transit Group</b>	<b>Total</b>
Balance at December 31, 2005	\$ 100,055	\$ 18,126	\$ 118,181
Foreign currency impact	579	510	1,089
<b>Balance at June 30, 2006</b>	<b>\$ 100,634</b>	<b>\$ 18,636</b>	<b>\$ 119,270</b>

**7. LONG-TERM DEBT**

Long-term debt consisted of the following:

<i>In thousands</i>	<b>June 30, 2006</b>	<b>December 31, 2005</b>
6.875% Senior Notes	\$ 150,000	\$ 150,000
<b>Total</b>	<b>\$ 150,000</b>	<b>\$ 150,000</b>
Less current portion		
<b>Long-term portion</b>	<b>\$ 150,000</b>	<b>\$ 150,000</b>

*Refinancing Credit Agreement*

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In January 2004, the Company refinanced its existing unsecured revolving credit agreement with a consortium of commercial banks. This Refinancing Credit Agreement provided a \$175 million five-year revolving credit facility expiring in January 2009. In November 2005, the Company entered into an amendment to the Refinancing Credit Agreement which, among other things, extended the expiration of the agreement until

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

December 2010. At June 30, 2006, the Company had available borrowing capacity, net of \$23.9 million of letters of credit, of approximately \$151.1 million, subject to certain financial covenant restrictions.

Refinancing Credit Agreement borrowings bear variable interest rates indexed to the indices described below. The Company did not borrow under the Refinancing Credit Agreement during the six months ended June 30, 2006 or during the year ended December 31, 2005.

Under the Refinancing Credit Agreement, the Company may elect a base interest rate or an interest rate based on the London Interbank Offered Rates of Interest ( LIBOR ). The base rate is the greater of LaSalle Bank National Association's prime rate or the federal funds effective rate plus 0.5% per annum. The LIBOR rate is based on LIBOR plus a margin that ranges from 62.5 to 175 basis points depending on the Company's consolidated total indebtedness to cash flow ratios. The current margin is 62.5 basis points.

The Refinancing Credit Agreement limits the Company's ability to declare or pay cash dividends and prohibits the Company from declaring or making other distributions, subject to certain exceptions. The Refinancing Credit Agreement contains various other covenants and restrictions including the following limitations: incurrence of additional indebtedness; mergers, consolidations and sales of assets and acquisitions; additional liens; sale and leasebacks; permissible investments, loans and advances; certain debt payments; capital expenditures; and imposes a minimum interest expense coverage ratio and a maximum debt to cash flow ratio.

The Refinancing Credit Agreement contains customary events of default, including payment defaults, failure of representations or warranties to be true in any material respect, covenant defaults, defaults with respect to other indebtedness of the Company, bankruptcy, certain judgments against the Company, ERISA defaults and change of control of the Company. The Refinancing Credit Agreement includes the following covenants: a minimum interest coverage ratio of three, maximum debt to cash flow ratio of 3.25 and a minimum net worth of \$180 million plus 50% of consolidated net income since September 30, 2003. The Company is in compliance with these measurements and covenants.

*6<sup>7</sup>/8% Senior Notes Due August 2013*

In August 2003, the Company issued \$150 million of Senior Notes due in 2013 ( Notes ). The Notes were issued at par. Interest on the Notes will accrue at a rate of 6.875% per annum and is payable semi-annually on January 31 and July 31 of each year. The proceeds were used to repay debt outstanding under the Company's existing credit agreement, and for general corporate purposes.

The Notes are senior unsecured obligations of the Company and rank pari passu with all existing and future senior debt and are senior to all our existing and future subordinated indebtedness of the Company. The indenture under which the Notes were issued contains covenants and restrictions which limit among other things, the following: the incurrence of indebtedness, payment of dividends and certain distributions, sale of assets, change in control, mergers and consolidations and the incurrence of liens.

On July 31, 2006, the Board of Directors authorized the repurchase of up to \$50 million of the Company's outstanding shares. The Company intends to purchase these shares on the open market or in negotiated or block trades. No time limit was set for the completion of the program which qualifies under the Refinancing Credit Agreement, as well as the 6<sup>7</sup>/8% Senior Notes currently outstanding.

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**8. EMPLOYEE BENEFIT PLANS**

The Company sponsors defined benefit pension plans that cover certain U.S., Canadian and United Kingdom employees and which provide benefits of stated amounts for each year of service of the employee.

<i>In thousands, except percentages</i>	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>Three months ended</b>		<b>Three months ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Net periodic benefit cost</b>				
Service cost	\$ 1,085	\$ 703	\$ 325	\$ 279
Interest cost	1,996	1,939	656	543
Expected return on plan assets	(2,169)	(1,954)		
Net amortization/deferrals	918	886	272	(368)
 Net periodic benefit cost	 \$ 1,830	 \$ 1,574	 \$ 1,253	 \$ 454

**Assumptions**

Discount rate	5.21%	5.94%	5.43%	6.20%
Expected long-term rate of return	6.96%	7.20%	NA	NA
Rate of compensation increase	3.38%	4.10%	NA	NA

<i>In thousands, except percentages</i>	<b>Pension Plans</b>		<b>Postretirement Plan</b>	
	<b>Six months ended</b>		<b>Six months ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Net periodic benefit cost</b>				
Service cost	\$ 2,153	\$ 1,647	\$ 648	\$ 476
Interest cost	3,967	3,903	1,310	1,206
Expected return on plan assets	(4,312)	(3,958)		
Net amortization/deferrals	1,828	1,902	543	482
 Net periodic benefit cost	 \$ 3,636	 \$ 3,494	 \$ 2,501	 \$ 2,164

**Assumptions**

Discount rate	5.21%	5.94%	5.43%	6.20%
Expected long-term rate of return	6.96%	7.20%	NA	NA
Rate of compensation increase	3.38%	4.10%	NA	NA

The Company's funding methods are based on governmental requirements and differ from those methods used to recognize pension expense. The Company expects to contribute \$9.4 million to the pension plans during 2006 but expects that this level of funding will decrease in future periods. Rebalancing of the asset allocation occurs on a quarterly basis.

In addition to providing pension benefits, the Company has provided certain unfunded postretirement health care and life insurance benefits for a portion of North American employees. The Company is not obligated to pay health care and life insurance benefits to individuals who had retired prior to 1990.



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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

**9. INCOME TAXES**

The overall effective income tax rate was 35.0% and 35.6% for the three and six months ended June 30, 2006 and 36.4% and 36.5% for the three and six months ended June 30, 2005, respectively.

**10. EARNINGS PER SHARE**

The computation of earnings per share is as follows:

<i>In thousands, except per share</i>	<b>Three Months Ended June 30,</b>	
	<b>2006</b>	<b>2005</b>
<b>Basic earnings per share</b>		
Income from continuing operations applicable to common shareholders	\$ 21,782	\$ 14,933
Divided by		
Weighted average shares outstanding	48,451	46,862
Basic earnings from continuing operations per share	\$ 0.45	\$ 0.32
<b>Diluted earnings per share</b>		
Income from continuing operations applicable to common shareholders	\$ 21,782	\$ 14,933
Divided by sum of the		
Weighted average shares outstanding	48,451	46,862
Conversion of dilutive stock options	641	682
Diluted shares outstanding	49,092	47,544
Diluted earnings from continuing operations per share	\$ 0.44	\$ 0.31

<i>In thousands, except per share</i>	<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2005</b>
<b>Basic earnings per share</b>		
Income from continuing operations applicable to common shareholders	\$ 41,850	\$ 24,276
Divided by		
Weighted average shares outstanding	48,210	46,452
Basic earnings from continuing operations per share	\$ 0.87	\$ 0.52
<b>Diluted earnings per share</b>		
Income from continuing operations applicable to common shareholders	\$ 41,850	\$ 24,276
Divided by sum of the		
Weighted average shares outstanding	48,210	46,452
Conversion of dilutive stock options	641	705
Diluted shares outstanding	48,851	47,157

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Diluted earnings from continuing operations per share	\$ 0.86	\$ 0.51
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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

**11. WARRANTIES**

The following table reconciles the changes in the Company's product warranty reserve:

<i>In thousands</i>	<b>Six Months Ended June 30.</b>	
	<b>2006</b>	<b>2005</b>
Balance at December 31, 2005 and 2004, respectively	\$ 16,158	\$ 17,413
Warranty provision	5,376	2,983
Warranty claim payments	(3,977)	(4,739)
Balance at June 30, 2006 and 2005, respectively	\$ 17,557	\$ 15,657

**12. COMMITMENTS AND CONTINGENCIES**

Claims have been filed against the Company and certain of its affiliates in various jurisdictions across the United States by persons alleging bodily injury as a result of exposure to asbestos-containing products. Since 2000, the number of such claims has increased and the resolution of these claims may take a significant period of time. Most of these claims have been made against our wholly owned subsidiary, Railroad Friction Products Corporation (RFPC), and are based on a product sold by RFPC prior to the time that the Company acquired any interest in RFPC. On April 17, 2005, a claim against the Company by a former stockholder of RFPC contending that the Company assumed that entity's liability for asbestos claims arising from exposure to RFPC's product was resolved in the Company's favor.

Most of these claims, including all of the RFPC claims, are submitted to insurance carriers for defense and indemnity or to non-affiliated companies that retain the liabilities for the asbestos-containing products at issue. We cannot, however, assure that all these claims will be fully covered by insurance or that the indemnitors will remain financially viable. Our ultimate legal and financial liability with respect to these claims, as is the case with other pending litigation, cannot be estimated.

It is Management's belief that the potential range of loss for asbestos-related bodily injury cases is not reasonably determinable at present for a variety of factors, including: (1) the limited asbestos case settlement history of the Company's wholly owned subsidiary, Railroad Friction Products Corporation (RFPC); (2) the unpredictable nature of personal injury litigation in general; and (3) the uncertainty of asbestos litigation in particular. Despite this uncertainty, and although the results of the Company's operations and cash flows for any given period could be adversely affected by asbestos-related lawsuits, Management believes that the final resolution of the Company's asbestos-related cases will not be material to the Company's overall financial position, results of operations and cash flows. In general, this belief is based upon: (1) Wabtec's and RFPC's limited history of settlements and dismissals of asbestos-related cases to date; (2) the inability of many plaintiffs to establish any exposure or causal relationship to RFPC's product; and (3) the inability of many plaintiffs to demonstrate any identifiable injury or compensable loss.

More specifically, as to RFPC, Management's belief that any losses due to asbestos-related cases would not be material is also based on the fact that RFPC owns insurance which provides coverage for asbestos-related bodily injury claims. To date, RFPC's insurers have provided RFPC with defense and indemnity in these actions. As to Wabtec and its divisions, Management's belief that asbestos-related cases will not have a material impact is also based on its position that it has no legal liability for asbestos-related bodily injury claims, and that the former owners of Wabtec's assets retained asbestos liabilities for the products at issue. To date, Wabtec has been able to successfully defend itself on this basis, including an arbitration decision and a judicial opinion, both of



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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

which confirmed Wabtec's position that it did not assume any asbestos liabilities from a former owner of a majority of Wabtec's assets. Although Wabtec has incurred defense and administrative costs in connection with asbestos bodily injury actions, these costs have not been material, and the company has no information that would suggest these costs would become material in the foreseeable future.

The GETS-GS litigation described in the Company's Annual Report on Form 10-K for the Year Ended December 31, 2005 was settled in April of 2006 for \$3.8 million, which had been reserved for in prior years.

In April 2005, Amtrak decided to suspend its Acela Express train service due to cracks in the spokes of some of the cars' brake discs. Amtrak's Acela service was resumed on a limited basis in July, 2005, and complete service was resumed in September, 2005. Wabtec did not design or supply the braking system for the Acela cars. The braking system was supplied by Knorr Brake Corporation and the brake discs were designed by Faiveley Transport. Wabtec did provide and machined approximately one-third of the brake discs for the cars and assisted Amtrak and others, including Bombardier Corporation, Alstom Transportation Inc., Knorr and Faiveley, in their evaluation and investigation of the brake disc cracks.

On July 11, 2005 Wabtec received a written notice of a potential claim for damages from Knorr and on March 2, 2006 received a notice from Knorr in which Knorr stated that Amtrak is of the view that it may have warranty claims against Wabtec, Knorr, and Faiveley. Neither Knorr notice specified any amount or range of claims against the Company, although Knorr has indicated that it expects the Company to participate in any financial settlement arising from the alleged defects and failures of the Acela brake discs. Wabtec, in turn, has forwarded Knorr's notices to Faiveley and has notified Faiveley of potential claims by Wabtec against Faiveley.

Bombardier recently reported to Wabtec and Faiveley that Bombardier and Knorr have incurred approximately \$48 million in costs and losses due to the suspension of Amtrak's Acela service, including the cost of compensating Amtrak. In turn, Wabtec has contacted Faiveley, asserting that Faiveley is fully responsible for the claims of Bombardier and Knorr. Wabtec does not believe that it has any material legal liability with regard to this matter.

In March 2006, management began an internal investigation related to business transactions conducted by a subsidiary, Pioneer Friction Limited (Pioneer), in West Bengal, India. Through an internal compliance review, management discovered that disbursements were made which may be in violation of applicable laws and regulations. Pioneer is a fourth-tier subsidiary of Wabtec; two of the intermediate subsidiaries are Australian companies which are, in turn, owned by a U.S. holding company.

While the transactions are inconsequential and not material to the overall operations of Wabtec, they may result in potential penalties. Management has concluded its initial investigation, and has notified Wabtec's Audit Committee, Board of Directors, and the appropriate authorities of its findings so far. Wabtec has not recorded a reserve related to this matter as of June 30, 2006; because the Company's potential exposure cannot be estimated based on management's current assessment of the situation.

The Company is subject to a number of other commitments and contingencies as described in its Annual Report on Form 10-K for the Year Ended December 31, 2005, filed on March 16, 2006. During the first six months of 2006, there were no material changes other than what is discussed above to the information described in Note 18 therein.

**Table of Contents****WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)****13. SEGMENT INFORMATION**

Wabtec has two reportable segments – the Freight Group and the Transit Group. The key factors used to identify these reportable segments are the organization and alignment of the Company's internal operations, the nature of the products and services, and customer type. The business segments are:

**Freight Group** manufactures products and provides services geared to the production and operation of freight cars and locomotives, including braking control equipment, on-board electronic components and train coupler equipment. Revenues are derived from OEM sales, aftermarket sales and freight car repairs and services.

**Transit Group** consists of products for passenger transit vehicles and locomotives (typically subways, commuter rail and buses) that include braking, coupling, monitoring systems, climate control and door equipment engineered to meet individual customer specifications. Revenues are derived from OEM and aftermarket sales as well as from repairs and services.

The Company evaluates its business segments' operating results based on income from operations. Corporate activities include general corporate expenses, elimination of intersegment transactions, interest income and expense and other unallocated charges. Since certain administrative and other operating expenses and other items have not been allocated to business segments, the results in the following tables are not necessarily a measure computed in accordance with generally accepted accounting principles and may not be comparable to other companies.

Beginning with the first quarter of 2006, the Company transferred certain operations from the Freight to the Transit Group to reflect a shift in the markets and customers served by those operations. For the three month period ended June 30, 2005, this reclassification increased Transit Group sales by about \$25 million and income from continuing operations before income taxes by \$4.4 million. For the six-month period ended June 30, 2005, this reclassification increased Transit Group sales by about \$41 million, and income from continuing operations before income taxes by \$5.3 million. Prior period results have been adjusted for comparability purposes.

Segment financial information for the three months ended June 30, 2006 is as follows:

<i>In thousands</i>	<b>Freight Group</b>	<b>Transit Group</b>	<b>Corporate Activities</b>	<b>Total</b>
Sales to external customers	\$ 187,751	\$ 74,151	\$	\$ 261,902
Intersegment sales/(elimination)	4,238	145	(4,383)	
<b>Total sales</b>	<b>\$ 191,989</b>	<b>\$ 74,296</b>	<b>\$ (4,383)</b>	<b>\$ 261,902</b>
Income (loss) from operations	\$ 41,237	\$ 4,291	\$ (9,982)	\$ 35,546
Interest expense and other			(2,043)	(2,043)
Income (loss) from continuing operations before income taxes	\$ 41,237	\$ 4,291	\$ (12,025)	\$ 33,503

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**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Segment financial information for the three months ended June 30, 2005 is as follows:

<i>In thousands</i>	<b>Freight Group</b>	<b>Transit Group</b>	<b>Corporate Activities</b>	<b>Total</b>
Sales to external customers	\$ 181,449	\$ 84,848	\$	\$ 266,297
Intersegment sales/(elimination)	2,169	82	(2,251)	
<b>Total sales</b>	<b>\$ 183,618</b>	<b>\$ 84,930</b>	<b>\$ (2,251)</b>	<b>\$ 266,297</b>
Income (loss) from operations	\$ 28,266	\$ 7,567	\$ (9,537)	\$ 26,296
Interest expense and other			(2,852)	(2,852)
Income (loss) from continuing operations before income taxes	\$ 28,266	\$ 7,567	\$ (12,389)	\$ 23,444

Segment financial information for the six months ended June 30, 2006 is as follows:

<i>In thousands</i>	<b>Freight Group</b>	<b>Transit Group</b>	<b>Corporate Activities</b>	<b>Total</b>
Sales to external customers	\$ 376,102	\$ 148,209	\$	\$ 524,311
Intersegment sales/(elimination)	7,525	262	(7,787)	
<b>Total sales</b>	<b>\$ 383,627</b>	<b>\$ 148,471</b>	<b>\$ (7,787)</b>	<b>\$ 524,311</b>
Income (loss) from operations	\$ 82,734	\$ 7,057	\$ (21,765)	\$ 68,026
Interest expense and other			(3,047)	(3,047)
Income (loss) from continuing operations before income taxes	\$ 82,734	\$ 7,057	\$ (24,812)	\$ 64,979

Segment financial information for the six months ended June 30, 2005 is as follows:

<i>In thousands</i>	<b>Freight Group</b>	<b>Transit Group</b>	<b>Corporate Activities</b>	<b>Total</b>
Sales to external customers	\$ 347,239	\$ 160,858	\$	\$ 508,097
Intersegment sales/(elimination)	4,623	140	(4,763)	
<b>Total sales</b>	<b>\$ 351,862</b>	<b>\$ 160,998</b>	<b>\$ (4,763)</b>	<b>\$ 508,097</b>
Income (loss) from operations	\$ 48,262	\$ 11,789	\$ (15,396)	\$ 44,655
Interest expense and other			(6,485)	(6,485)

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Income (loss) from continuing operations before income taxes	\$ 48,262	\$ 11,789	\$ (21,881)	\$ 38,170
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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
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Sales by Product for the three months ended June 30, is as follows:

<i>In thousands</i>	<b>Three Months Ended June 30.</b>	
	<b>2006</b>	<b>2005</b>
Brake Products	\$ 99,965	\$ 93,260
Freight Electronics & Specialty Products	79,056	84,675
Remanufacturing, Overhaul & Build	47,637	58,921
Transit Products	26,725	28,437
Other	8,519	1,004
Total Sales	\$ 261,902	\$ 266,297

Sales by Product for the six months ended June 30, is as follows:

<i>In thousands</i>	<b>Six Months Ended June 30.</b>	
	<b>2006</b>	<b>2005</b>
Brake Products	\$ 202,160	\$ 180,334
Freight Electronics & Specialty Products	162,533	160,107
Remanufacturing, Overhaul & Build	90,847	96,357
Transit Products	54,628	64,446
Other	14,143	6,853
Total Sales	\$ 524,311	\$ 508,097

#### **14. GUARANTOR SUBSIDIARIES FINANCIAL INFORMATION**

Effective August 2003, the Company issued \$150 million of Senior Notes due in 2013 ( Notes ). The obligations under the Notes are fully and unconditionally guaranteed by all U.S. subsidiaries as guarantors. In accordance with positions established by the Securities and Exchange Commission, the following shows separate financial information with respect to the parent, the guarantor subsidiaries and the non-guarantor subsidiaries. The principal elimination entries eliminate investment in subsidiaries and certain intercompany balances and transactions.

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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Balance Sheet as of June 30, 2006:

<i>In thousands</i>	Parent	Guarantors	Non-Guarantors	Elimination	Consolidated
Cash	\$ 166,524	\$ (6,492)	\$ 78,875	\$	\$ 238,907
Accounts Receivable	166	98,309	64,518		162,993
Inventories		93,703	46,034		139,737
Other Current Assets	19,390	5,539	3,127		28,056
Total Current Assets	186,080	191,059	192,554		569,693
Net Property, Plant and Equipment	3,143	95,855	65,498		164,496
Goodwill	8,521	76,729	34,020		119,270
Investment in Subsidiaries	874,971	155,202	24,755	(1,054,928)	
Intangibles	9,000	24,278	4,822		38,100
Other Long Term Assets	13,353	2,577	12,960		28,890
Total Assets	\$ 1,095,068	\$ 545,700	\$ 334,609	\$ (1,054,928)	\$ 920,449
Current Liabilities	\$ 16,888	\$ 171,588	\$ 66,969	\$	\$ 255,445
Intercompany	232,663	(267,366)	34,703		
Long-Term Debt	150,000				150,000
Other Long Term Liabilities	241,672	(190,243)	9,730		61,159
Total Liabilities	641,223	(286,021)	111,402		466,604
Stockholders' Equity	453,845	831,721	223,207	(1,054,928)	453,845
Total Liabilities and Stockholders' Equity	\$ 1,095,068	\$ 545,700	\$ 334,609	\$ (1,054,928)	\$ 920,449



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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Balance Sheet as of December 31, 2005:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination</b>	<b>Consolidated</b>
Cash	\$ 87,899	\$ (2,758)	\$ 56,224	\$	\$ 141,365
Accounts Receivable	145	135,281	71,465		206,891
Inventories		73,419	37,454		110,873
Other Current Assets	17,519	2,195	4,083		23,797
<b>Total Current Assets</b>	<b>105,563</b>	<b>208,137</b>	<b>169,226</b>		<b>482,926</b>
Net Property, Plant and Equipment	3,843	93,108	64,650		161,601
Goodwill	8,521	76,728	32,932		118,181
Investment in Subsidiaries	781,663	155,201	24,755	(961,619)	
Intangibles	9,396	24,982	4,751		39,129
Other Long Term Assets	13,980	9,806	10,734		34,520
<b>Total Assets</b>	<b>\$ 922,966</b>	<b>\$ 567,962</b>	<b>\$ 307,048</b>	<b>\$ (961,619)</b>	<b>\$ 836,357</b>
<b>Current Liabilities</b>	<b>\$ 19,287</b>	<b>\$ 155,992</b>	<b>\$ 66,200</b>	<b>\$</b>	<b>\$ 241,479</b>
Intercompany	320,568	(348,912)	28,344		
Long-Term Debt	150,000				150,000
Other Long Term Liabilities	53,904	3,065	8,702		65,671
<b>Total Liabilities</b>	<b>543,759</b>	<b>(189,855)</b>	<b>103,246</b>	<b>(961,619)</b>	<b>457,150</b>
Stockholders' Equity	379,207	757,817	203,802	(961,619)	379,207
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 922,966</b>	<b>\$ 567,962</b>	<b>\$ 307,048</b>	<b>\$ (961,619)</b>	<b>\$ 836,357</b>

Income Statement for the Three Months Ended June 30, 2006:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination(1)</b>	<b>Consolidated</b>
Net Sales	\$	\$ 194,416	\$ 96,781	\$ (29,295)	\$ 261,902
Cost of Sales	(449)	(131,218)	(78,193)	24,699	(185,161)
<b>Gross Profit (Loss)</b>	<b>(449)</b>	<b>63,198</b>	<b>18,588</b>	<b>(4,596)</b>	<b>76,741</b>
Operating Expenses	(12,167)	(20,613)	(8,415)		(41,195)
<b>Operating Profit (Loss)</b>	<b>(12,616)</b>	<b>42,585</b>	<b>10,173</b>	<b>(4,596)</b>	<b>35,546</b>
Interest (Expense) Income	(4,125)	3,150	555		(420)
Other (Expense) Income	(34)	444	(2,033)		(1,623)
Equity Earnings	42,569	(2,990)		(39,579)	
	25,794	43,189	8,695	(44,175)	33,503

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Income (Loss) From Continuing Operations Before Income Taxes					
Income Tax Benefit (Expense)	(4,925)	(3,949)	(2,847)		(11,721)
Income (Loss) From Continuing Operations	20,869	39,240	5,848	(44,175)	21,782
Discontinued Operations	276	27	(940)		(637)
Net Income (Loss)	\$ 21,145	\$ 39,267	\$ 4,908	\$ (44,175)	\$ 21,145

(1) Includes elimination of gross profit realized with certain intercompany transactions between Guarantor and Non-Guarantor subsidiaries.

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Income Statement for the Three Months Ended June 30, 2005:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination(1)</b>	<b>Consolidated</b>
Net Sales	\$	\$ 191,783	\$ 112,481	\$ (37,967)	\$ 266,297
Cost of Sales	916	(145,518)	(87,935)	32,415	(200,122)
Gross Profit (Loss)	916	46,265	24,546	(5,552)	66,175
Operating Expenses	(8,805)	(21,188)	(9,886)		(39,879)
Operating Profit (Loss)	(7,889)	25,077	14,660	(5,552)	26,296
Interest (Expense) Income	(5,004)	2,826	13		(2,165)
Other (Expense) Income	(1,730)	1,812	(769)		(687)
Equity Earnings	29,683	3,652		(33,335)	
Income (Loss) From Continuing Operations Before Income Taxes	15,060	33,367	13,904	(38,887)	23,444
Income Tax Benefit (Expense)	91	(3,823)	(4,779)		(8,511)
Income (Loss) From Continuing Operations	15,151	29,544	9,125	(38,887)	14,933
Discontinued Operations			218		218
Net Income (Loss)	\$ 15,151	\$ 29,544	\$ 9,343	\$ (38,887)	\$ 15,151

(1) Includes elimination of gross profit realized with certain intercompany transactions between Guarantor and Non-Guarantor subsidiaries.  
Income Statement for the Six Months Ended June 30, 2006:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination(1)</b>	<b>Consolidated</b>
Net Sales	\$	\$ 394,372	\$ 196,274	\$ (66,335)	\$ 524,311
Cost of Sales	288	(271,234)	(157,919)	56,385	(372,480)
Gross Profit (Loss)	288	123,138	38,355	(9,950)	151,831
Operating Expenses	(25,621)	(40,999)	(17,185)		(83,805)
Operating Profit (Loss)	(25,333)	82,139	21,170	(9,950)	68,026
Interest (Expense) Income	(8,667)	6,122	1,001		(1,544)
Other (Expense) Income	(380)	781	(1,904)		(1,503)
Equity Earnings	83,569	(5,144)		(78,425)	
Income (Loss) From Continuing Operations Before Income Taxes	49,189	83,898	20,267	(88,375)	64,979

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Income Tax Benefit (Expense)	(8,274)	(8,012)	(6,843)		(23,129)
Income (Loss) From Continuing Operations	40,915	75,886	13,424	(88,375)	41,850
Discontinued Operations	276		(935)		(659)
Net Income (Loss)	\$ 41,191	\$ 75,886	\$ 12,489	\$ (88,375)	\$ 41,191

(1) Includes elimination of gross profit realized with certain intercompany transactions between Guarantor and Non-Guarantor subsidiaries.

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Income Statement for the Six Months Ended June 30, 2005:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination(1)</b>	<b>Consolidated</b>
Net Sales	\$	\$ 370,467	\$ 209,609	\$ (71,979)	\$ 508,097
Cost of Sales	2,173	(281,186)	(167,570)	61,673	(384,910)
Gross Profit (Loss)	2,173	89,281	42,039	(10,306)	123,187
Operating Expenses	(19,104)	(41,120)	(18,308)		(78,532)
Operating Profit (Loss)	(16,931)	48,161	23,731	(10,306)	44,655
Interest (Expense) Income	(9,115)	4,551	(85)		(4,649)
Other (Expense) Income	(2,098)	2,530	(2,268)		(1,836)
Equity Earnings	51,108	5,910		(57,018)	
Income (Loss) From Continuing Operations Before Income Taxes	22,964	61,152	21,378	(67,324)	38,170
Income Tax Benefit (Expense)	1,435	(7,648)	(7,681)		(13,894)
Income (Loss) From Continuing Operations	24,399	53,504	13,697	(67,324)	24,276
Discontinued Operations			123		123
Net Income (Loss)	\$ 24,399	\$ 53,504	\$ 13,820	\$ (67,324)	\$ 24,399

(1) Includes elimination of gross profit realized with certain intercompany transactions between Guarantor and Non-Guarantor subsidiaries.  
Condensed Statement of Cash Flows for the Six Months Ended June 30, 2006:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination</b>	<b>Consolidated</b>
Net Cash Provided by (Used in) Operating Activities	\$ 65,817	\$ 78,306	\$ 17,749	\$ (88,375)	\$ 73,497
Net Cash (Used in) Provided by Investing Activities	(333)	(6,154)	536		(5,951)
Net Cash Provided by (Used in) Financing Activities	13,141	(75,886)	(12,489)	88,375	13,141
Effect of Changes in Currency Exchange Rates			16,855		16,855
Increase (Decrease) in Cash	78,625	(3,734)	22,651		97,542
Cash at Beginning of Period	87,899	(2,758)	56,224		141,365
Cash at End of Period	\$ 166,524	\$ (6,492)	\$ 78,875	\$	\$ 238,907

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**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006 (UNAUDITED)**

Condensed Statement of Cash Flows for the Six Months Ended June 30, 2005:

<i>In thousands</i>	<b>Parent</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Elimination</b>	<b>Consolidated</b>
Net Cash Provided by (Used in) Operating Activities	\$ 6,008	\$ 68,327	\$ 23,127	\$ (67,324)	\$ 30,138
Net Cash Used in Investing Activities	(367)	(42,523)	(3,994)		(46,884)
Net Cash Provided by (Used in) Financing Activities	15,719	(53,552)	(13,879)	67,324	16,651
Effect of Changes in Currency Exchange Rates			(7,271)		(7,271)
Increase (Decrease) in Cash	21,360	(27,748)	(2,017)		(8,405)
Cash at Beginning of Period	41,117	24,849	29,291		95,257
Cash at End of Period	\$ 62,477	\$ (2,899)	\$ 27,274	\$	\$ 86,852

**15. OTHER EXPENSE**

The components of other expense are as follows:

<i>In thousands</i>	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Foreign currency loss	\$ 1,316	\$ 637	\$ 930	\$ 1,613
Other miscellaneous expense	307	50	573	223
Total other expense	\$ 1,623	\$ 687	\$ 1,503	\$ 1,836

**Table of Contents****Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion should be read in conjunction with the information in the unaudited condensed consolidated financial statements and notes thereto included herein and Westinghouse Air Brake Technologies Corporation's Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in its 2005 Annual Report on Form 10-K, filed March 16, 2006.*

**OVERVIEW**

Wabtec is one of the world's largest providers of value-added, technology-based products and services for the global rail industry. Our products are found on virtually all U.S. locomotives, freight cars and passenger transit vehicles, as well as in more than 80 countries throughout the world. Our products enhance safety, improve productivity and reduce maintenance costs for customers, and many of our core products and services are essential in the safe and efficient operation of freight rail and passenger transit vehicles. Wabtec is a global company with operations in 11 countries. In the first half of 2006, about 32 percent of the Company's revenues came from outside the U.S.

*Management Review and Outlook*

Wabtec's long-term financial goals are to generate free cash flow in excess of net income, maintain a strong credit profile while minimizing our overall cost of capital, increase margins through strict attention to cost controls, and increase revenues through a focused growth strategy. In addition, management monitors the Company's short-term operational performance through measures such as quality and on-time delivery.

Freight rail industry statistics, such as carloadings and orders for new freight cars, are continuing to improve in 2006. Deliveries of new freight cars increased to 68,657 in 2005, and orders increased to 80,703. As a result, at year-end the backlog of freight cars ordered was 69,408. This trend continued in the first half of 2006, with orders climbing to 54,181, deliveries of 38,008, and a backlog of 85,692. Sales in our freight segment have benefited from that trend. Following are quarterly freight car statistics for the past three years:

	<b>Orders</b>	<b>Deliveries</b>	<b>Backlog*</b>
First quarter 2004	17,962	10,012	42,242
Second quarter 2004	19,770	10,071	51,446
Third quarter 2004	20,315	11,790	61,052
Fourth quarter 2004	12,244	14,419	58,677
	70,291	46,292	
First quarter 2005	17,563	15,781	59,416
Second quarter 2005	19,132	17,914	60,544
Third quarter 2005	17,439	16,987	60,986
Fourth quarter 2005	26,569	17,975	69,408
	80,703	68,657	
First quarter 2006	35,991	18,542	86,857
Second quarter 2006	18,190	19,466	85,692

Deliveries of transit cars were 918 and 819 for the years ended December 31, 2005 and 2004, respectively. Deliveries of locomotives were 1,106 and 1,202 for the years ended December 31, 2005 and 2004, respectively.

*Source: Railway Supply Institute and Management Estimates (\* Figures that do not rollforward period to period reflect minor adjustments subsequent to that period from figures reported by the Railway Supply Institute.)*

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Carloadings and Intermodal Units Originated have increased over the past three years reflecting higher rail traffic and ultimately better opportunities for maintenance and aftermarket sales for the Company:

**Carloadings Originated (in thousands):**

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
2004	4,296	4,327	4,267	4,171	17,061
2005	4,403	4,366	4,309	4,135	17,213
2006	4,338	4,453	n/a	n/a	n/a

**Intermodal Units Originated (in thousands):**

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
2004	2,585	2,750	2,810	2,849	10,994
2005	2,781	2,885	2,992	3,036	11,694
2006	2,937	3,093	n/a	n/a	n/a

Source: Association of American Railroads Weekly Rail Traffic

In addition to this cyclical rebound in orders and rail traffic, we expect to generate future increases in sales and earnings from executing our four-point growth strategy:

Global and Market Expansion;

Aftermarket Products and Services;

New Products and Technologies; and

Acquisitions.

In 2006 and beyond, we will continue to face many challenges, including increased costs for raw materials, especially steel; higher costs for medical and insurance premiums; and foreign currency fluctuations. In addition, we face general economic risks, as well as the risk that our customers could curtail spending on new and existing equipment. Risks associated with our four-point growth strategy include the level of investment that customers are willing to make in new technologies developed by the industry and the Company, and risks inherent in global expansion. When necessary, we will modify our financial and operating strategies to reflect changes in market conditions and risks.

On July 19, 2006, the Board of Directors approved a restructuring plan to improve the profitability and efficiency of certain business units. As part of the plan, Wabtec will downsize two of its Canadian plants, in Stoney Creek and Wallaceburg, by moving certain products to lower-cost facilities and outsourcing. The restructuring plan will result in the recognition of \$11 million in expenses, pre-tax, primarily for pension-related curtailment and settlement charges and fixed asset write downs for idled assets. These expenses will be recognized in the second half of 2006 and the first half of 2007.



**Table of Contents****RESULTS OF OPERATIONS**

The following table shows our Consolidated Statements of Operations for the periods indicated.

<i>In millions</i>	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net sales	\$ 261.9	\$ 266.3	\$ 524.3	\$ 508.1
Cost of sales	(185.2)	(200.1)	(372.5)	(384.9)
Gross profit	76.7	66.2	151.8	123.2
Selling, general and administrative expenses	(32.3)	(30.6)	(66.0)	(59.6)
Engineering expenses	(8.0)	(8.2)	(16.1)	(16.9)
Amortization expense	(0.9)	(1.1)	(1.7)	(2.0)
Total operating expenses	(41.2)	(39.9)	(83.8)	(78.5)
Income from operations	35.5	26.3	68.0	44.7
Interest expense, net	(0.4)	(2.2)	(1.5)	(4.7)
Other expense, net	(1.6)	(0.7)	(1.5)	(1.8)
Income from continuing operations before income taxes	33.5	23.4	65.0	38.2
Income tax expense	(11.7)	(8.5)	(23.1)	(13.9)
Income from continuing operations	21.8	14.9	41.9	24.3
Income (loss) from discontinued operations	(0.7)	0.3	(0.7)	0.1
Net income	\$ 21.1	\$ 15.2	\$ 41.2	\$ 24.4

**SECOND QUARTER 2006 COMPARED TO SECOND QUARTER 2005**

The following table summarizes the results of operations for the period:

<i>In thousands</i>	Three months ended June 30,		Percent Change
	2006	2005	
Net sales	\$ 261,902	\$ 266,297	-1.7%
Income from operations	33,503	23,444	42.9%
Net income	21,145	15,151	39.6%

Net sales decreased by \$4.4 million to \$261.9 from \$266.3 million for the three months ended June 30, 2006 and 2005, respectively. The decrease is primarily related to 2005 contract sales for the renovation of air conditioning units for transit cars of about \$6 million, and modules provided under a locomotive supply contract of about \$5 million that were not realized in 2006. However, the Company increased sales of freight components by about \$6 million due to strong freight car deliveries and demand for locomotive components. The Company did not realize any significant net sales improvement because of price increases or foreign exchange. Net income for the three months ended June 30, 2006 was \$21.1 million or \$0.43 per diluted share. Net income for the three months ended June 30, 2005 was \$15.1 million or \$0.32 per diluted share. This increase in net income was primarily due to improved profitability on the Company's locomotive modules contract, higher than anticipated steel and other material expenses in 2005 that management was not able to pass on to customers in the way of surcharges, offset by stock based compensation expense recognized under SFAS 123(R).

**Net sales** Beginning with the first quarter of 2006, the Company transferred certain operations from the Freight to Transit Group to reflect a shift in the markets and customers served by those operations. Prior period results have been adjusted for comparability purposes. For the three-month period ended June 30, 2006, this



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reclassification increased Transit Group sales by about \$24 million. The following table shows the Company's net sales by business segment:

<i>In thousands</i>	Three months ended June 30,	
	2006	2005
Freight Group	\$ 187,751	\$ 181,449
Transit Group	74,151	84,848
Net sales	\$ 261,902	\$ 266,297

Net sales for the three months ended June 30, 2006, decreased \$4.4 million, or -1.7%, as compared to three months ended June 30, 2005. The Freight Group's increased sales of \$6.3 million reflected higher sales of aftermarket parts of \$4.5 million; higher demand for pneumatic air brake components related to increased deliveries of freight cars of \$6.5 million; offset by a \$5 million decrease in sales from a locomotive module contract. Industry deliveries of new freight cars for the second quarter of 2006 increased to 19,466 units as compared to 17,914 for the 2<sup>nd</sup> quarter 2005. As long as freight car deliveries and freight car loadings continue to increase, similar positive trends are expected to be realized by the Company. Transit Group sales were lower mostly by \$10.7 million due to a contract completed in 2005 to renovate air conditioning systems for transit cars resulting in a decrease in revenue of \$6 million, and \$4.4 million decline in transit revenue demand while certain large transit car contracts ramp up for 2007. As transit car deliveries for certain large transit authorities begin to increase in late 2006 and 2007, sales volume is expected to increase.

**Gross profit** Gross profit increased to \$76.7 million in the second quarter of 2006 compared to \$66.2 million in the same period of 2005. Gross profit is dependent on a number of factors including pricing, sales volume and product mix. In the second quarter of 2006, gross profit, as a percentage of sales, was 29.3% compared to 24.9% in 2005. This increase in gross profit percentage is due to a variety of factors including improved performance of a locomotive module contract which was profitable for the three months ended June 30, 2006, compared to a loss in the prior year same period. For the three months ended June 30, 2006, the locomotive module contract overall improvement was \$6.2 million from the losses realized in the prior year. The remaining improvement is due to cost savings realized from sourcing raw materials from lower cost suppliers, reduced labor costs, and continuing improvements in our manufacturing processes.

The provision for warranty expense was \$1.8 million higher for the second quarter of 2006 compared to the same period in the prior year, which negatively impacted gross profit. The most significant reason for the increase is due to specific reserves related to certain freight components and electronic products manufactured at our U.S. plants. In general, reserves, which are established based on historical claims as a percentage of revenue, were higher for locomotive manufacture and overhaul business unit. Sales have increased resulting in a higher reserve compared to prior quarter. Overall, our warranty reserve increased at June 30, 2006 compared to June 30, 2005 by \$2.0 million as reserves were established before claims were paid related to specific and general provisions discussed above.

**Operating expenses** The following table shows our operating expenses:

<i>In thousands</i>	Three months ended June 30, Percent		
	2006	2005	Change
Selling, general and administrative expenses	\$ 32,313	\$ 30,623	5.5%
Engineering expenses	8,023	8,183	(2.0)%
Amortization expense	859	1,073	(19.9)%
Total operating expenses	\$ 41,195	\$ 39,879	3.3%

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Operating expenses increased \$1.3 million in the second quarter of 2006 compared to the same period of 2005. These expenses were 15.7% and 15.0% of sales for the quarters ended June 30, 2006 and 2005, respectively. The increase is due to expense recognized in connection with the adoption of SFAS 123(R) and certain other share-based compensation accruals for long-term incentive plans. Stock based compensation was \$1.6 million and \$474,000 for the three months ended June 30, 2006 and 2005, respectively. The primary reason for the increase in stock based compensation expense between years is the issuance of shares in 2006 under a non-vested stock plan and increased expense under a stock based incentive plan as a result of the improved performance of the Company.

**Income from operations** Income from operations totaled \$33.5 million (or 13.6% of sales) in the second quarter of 2006 compared with \$26.3 million (or 9.9% of sales) in the same period of 2005. The increase is due primarily to the improved gross margin on current period sales, offset by increased operating costs specific to the adoption of SFAS 123(R).

**Interest expense, net** Interest expense, net decreased 80.6% in the second quarter of 2006 compared to the same period of 2005 primarily due to the Company's overall higher cash balances and rising interest rates, resulting in higher interest income.

**Other income (expense), net** The Company recorded foreign exchange loss of \$1.3 million and \$637,000, in the three months ended June 30, 2006 and 2005, respectively, due to the effect of currency exchange rate changes on intercompany transactions that are non U.S. dollar denominated amounts and charged or credited to earnings.

**Income taxes** The effective income tax rate was 35.0% and 36.4% for the second quarter of 2006 and 2005, respectively.

**Net income** Net income for the second quarter of 2006 increased \$5.9 million, compared with the same period of 2005. The increase due primarily to the improved gross margin on current period sales, decreased interest expense, net, and lower income taxes, offset by increased operating costs specific to the adoption of SFAS 123(R).

**FIRST SIX MONTHS OF 2006 COMPARED TO FIRST SIX MONTHS OF 2005**

The following table summarizes the results of operations for the period:

<i>In thousands</i>	Six months ended June 30,		Percent Change
	2006	2005	
Net sales	\$ 524,311	\$ 508,097	3.2%
Income from operations	64,979	38,170	70.2%
Net income	41,191	24,399	68.8%

Net sales increased by 3.2% from \$508.1 million in the first six months of 2005 to \$524.3 million in the same period in 2006. The increase is due to increased sales of freight components of about \$38 million related to strong freight car deliveries and demand for locomotive components, which was offset by decreased contract sales compared to the six month period ended June 30, 2005, for the renovation of air conditioning units for transit cars of about \$14 million, and modules provided under a locomotive supply contract of about \$8 million. Net income for the first six months of 2006 was \$41.2 million or \$0.84 per diluted share. Net income for the same period of 2005 was \$24.4 million or \$0.52 per diluted share. This increase in net income was primarily due to increased sales volume, improved profitability on the Company's locomotive modules contract, offset by stock based compensation expense recognized under SFAS 123(R).

**Net sales** Beginning with the first quarter of 2006, the Company transferred certain operations from the Freight to the Transit Group to reflect a shift in the markets and customers served by those operations. Prior

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period results have been adjusted for comparability purposes. For the six months ended June 30, 2006, this reclassification increased Transit Group sales by about \$41 million. The following table shows the Company's net sales by business segment:

<i>In thousands</i>	Six months ended	
	June 30, 2006	2005
Freight Group	\$ 376,102	\$ 347,239
Transit Group	148,209	160,858
Net sales	\$ 524,311	\$ 508,097

Net sales for the first six months of 2006 increased \$16.2 million, or 3.2%, as compared to the same period of 2005. The Freight Group's increased sales reflected higher sales of aftermarket parts of \$5.9 million; higher demand for pneumatic air brake components related to increased deliveries of freight cars of \$31.2 million; offset by a \$8 million decrease in sales from a locomotive module contract. Industry deliveries of new freight cars for the first half of 2006 increased to 38,008 units as compared to 33,695 for the first half of 2005. As long as freight car deliveries and freight car loadings continue to increase, similar positive trends are expected to be realized by the Company. Transit Group sales were lower mostly due to a 2005 non-recurring contract to renovate air conditioning systems for transit cars resulting in a decrease in revenue of \$14 million, and overall decline in transit revenue demand while certain large transit car contracts ramp up for 2007. As transit car deliveries for certain large transit authorities begin to increase in late 2006 and 2007, sales volume is expected to increase.

**Gross profit** Gross profit increased to \$151.8 million for the first six months of 2006 compared to \$123.2 million in the same period of 2005. Gross profit is dependent on a number of factors including pricing, sales volume and product mix. In the first half of 2006, gross profit, as a percentage of sales, was 29.0% compared to 24.2% in 2005. This increase in gross profit percentage is due to a variety of factors including improved performance of a locomotive module contract which was profitable for the six months ended June 30, 2006, compared to a loss in the prior year same period. The locomotive module contract overall improvement was \$11 million from the losses realized in the prior year. In the first six months of 2005, the Company recorded \$2.3 million in restructuring and asset impairment charges related to consolidating two U.K. facilities into one, relocating a product line from Canada to the U.S., and completion of a data center migration. The remaining improvement is due to costs savings realized from sourcing raw materials from lower cost suppliers, reduced labor costs, and continuing improvements in our manufacturing processes.

The provision for warranty expense was \$2.4 million higher for the first half of 2006 compared to the same period in the prior year, which negatively impacted gross profit. The most significant reason for the increase is due to specific reserves related to certain freight components and electronic products manufactured at our U.S. plants. In general, reserves, which are established based on historical claims as a percentage of revenue, were higher for locomotive manufacture and overhaul business unit. Sales have increased resulting in a higher reserve compared to prior quarter. Overall, our warranty reserve increased at June 30, 2006 compared to June 30, 2005 by \$2.0 million as reserves were established before claims were paid related to specific provisions discussed above.

**Operating expenses** The following table shows our operating expenses:

<i>In thousands</i>	Six months ended June 30, Percent		
	2006	2005	Change
Selling, general and administrative expenses	\$ 65,941	\$ 59,635	10.6%
Engineering expenses	16,138	16,853	(4.2)%
Amortization expense	1,726	2,044	(15.6)%
Total operating expenses	\$ 83,805	\$ 78,532	6.7%



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Operating expenses increased \$5.3 million in the first six months of 2006 compared to the same period of 2005. These expenses were 16.0% and 15.5% of sales for the first six months ended June 30, 2006 and 2005, respectively. The increase is due to expense recognized in connection with the adoption of SFAS 123(R) and certain other share-based compensation accruals for long-term incentive plans. During 2005, operating expenses included an information technology asset write-off of \$1.1 million. Stock based compensation was \$6 million and \$625,000 for the six months ended June 30, 2006 and 2005, respectively. The primary reason for the increase in stock based compensation expense between years is the issuance of shares in 2006 under a non-vested stock plan and increased expense under a stock based incentive plan as a result of the improved performance of the Company.

**Income from operations** Income from operations totaled \$68.0 million (or 13.0% of sales) in the first six months of 2006 compared with \$44.7 million (or 8.8% of sales) in the same period of 2005. The increase is due primarily to the improved gross margin on current period sales, offset by increased operating costs specific to the adoption of SFAS 123(R).

**Interest expense, net** Interest expense, net decreased 66.8% in the first six months of 2006 compared to the same period of 2005 primarily due to the Company's overall higher cash balances and rising interest rates, resulting in higher interest income.

**Other income (expense), net** The Company recorded foreign exchange loss of \$900,000 and \$1.6 million in the six months ended June 30, 2006 and 2005, respectively, due to the effect of currency exchange rate changes on intercompany transactions that are non U.S. dollar denominated amounts and charged or credited to earnings.

**Income taxes** The effective income tax rate was 35.6% and 36.5% for the first six months of 2006 and 2005, respectively.

**Net income** Net income for the first six months of 2006 increased \$16.8 million, compared with the same period of 2005. The increase due primarily to the improved gross margin on current period sales, decreased interest expense, net, and lower income taxes, offset by increased operating costs specific to the adoption of SFAS 123(R).

**Liquidity and Capital Resources**

Liquidity is provided primarily by operating cash flow and borrowings under the Company's unsecured credit facility with a consortium of commercial banks. The following is a summary of selected cash flow information and other relevant data.

<i>In thousands</i>	Six months ended	
	2006	June 30, 2005
Cash provided (used) by:		
Operating activities	\$ 73,497	\$ 30,289
Investing activities	(5,951)	(46,884)
Financing activities	13,141	15,461
Net Change in Cash	97,542	(8,405)

**Operating activities** Cash provided by operations in the first six months of 2006 was \$73 million as compared to \$30 million in the same period of 2005. This \$43 million increase was the result of increased earnings as well as certain changes in operating assets and liabilities. Net income for the Company increased \$21.8 million primarily as a result of higher gross profit with relatively stable sales levels. Cash provided by accounts receivable improved operating cash flows by \$59 million, and was the result of the Company collecting large customer receivables in 2006 for certain locomotive contracts. In particular, customer deposits from certain

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locomotive contracts accounted for the majority of the cash provided from operations. Inventory reduced operating cash flows by \$15.2 million compared to the first half of 2005. This inventory increase was anticipated since it was related to the same locomotive contracts as the units to be provided are in an initial start-up phase. Accrued income taxes increased operating cash flows by \$12 million due to the timing of tax payments. Accounts payable and accrued liabilities were a use of cash by about \$39.6 million compared to the prior period as accounts payable and other certain liabilities were reduced based on the timing of certain payments.

**Investing activities** In the first six months of 2006 and 2005, cash used in investing activities was \$6.0 million and \$46.9 million, respectively. In 2005, The Company acquired the assets of Rütgers Rail S.p.A. for \$35.6 million, net of cash received. Capital expenditures were \$9.0 million and \$11.5 million in the first six months of 2006 and 2005, respectively. The majority of capital expenditures for these periods relates to upgrades to and replacement of existing equipment.

**Financing activities** In the first six months of 2006 and 2005, cash provided by financing activities was \$13.1 million and \$15.6 million, respectively. The cash provided in 2006 included \$9.9 million of proceeds from the issuance of treasury stock for stock options and other benefit plans, offset by \$970,000 of dividend payments. The cash provided in 2005 included \$17.1 million of proceeds from the issuance of treasury stock for stock options and other benefit plans, offset by \$932,000 of dividend payments.

The following table shows our outstanding indebtedness at June 30, 2006 and December 31, 2005. The other term loan interest rates are variable and dependent on market conditions.

	June 30,	December 31,
<i>In thousands</i>	2006	2005
6.875% Senior notes due 2013	\$ 150,000	\$ 150,000
Total	\$ 150,000	\$ 150,000
Less-current portion		
Long-term portion	\$ 150,000	\$ 150,000

Cash balance at June 30, 2006 and December 31, 2005 was \$238.9 million and \$141.4 million, respectively.

**Refinancing Credit Agreement**

In January 2004, the Company refinanced its existing unsecured revolving credit agreement with a consortium of commercial banks. This Refinancing Credit Agreement provided a \$175 million five-year revolving credit facility expiring in January 2009. In November 2005, the Company entered into an amendment to the Refinancing Credit Agreement which, among other things, extended the expiration of the agreement until December 2010. At June 30, 2006, the Company had available bank borrowing capacity, net of \$23.9 million of letters of credit, of approximately \$151.1 million, subject to certain financial covenant restrictions.

Refinancing Credit Agreement borrowings bear variable interest rates indexed to the indices described below. The Company did not borrow under the Refinancing Credit Agreement during the six months ended June 30, 2006 or during the year ended December 31, 2005.

Under the Refinancing Credit Agreement, the Company may elect a base interest rate or an interest rate based on the London Interbank Offered Rates of Interest ( LIBOR ). The base interest rate is the greater of LaSalle Bank National Association's prime rate or the federal funds effective rate plus 0.5% per annum. The LIBOR rate is based on LIBOR plus a margin that ranges from 62.5 to 175 basis points depending on the Company's consolidated total indebtedness to cash flow ratios. The current margin is 62.5 basis points.



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The Refinancing Credit Agreement limits the Company's ability to declare or pay cash dividends and prohibits the Company from declaring or making other distributions, subject to certain exceptions. The Refinancing Credit Agreement contains various other covenants and restrictions including the following limitations: incurrence of additional indebtedness; mergers, consolidations and sales of assets and acquisitions; additional liens; sale and leasebacks; permissible investments, loans and advances; certain debt payments; capital expenditures; and imposes a minimum interest expense coverage ratio and a maximum debt to cash flow ratio.

The Refinancing Credit Agreement contains customary events of default, including payment defaults, failure of representations or warranties to be true in any material respect, covenant defaults, defaults with respect to other indebtedness of the Company, bankruptcy, certain judgments against the Company, ERISA defaults and change of control of the Company. The Refinancing Credit Agreement includes the following covenants: a minimum interest coverage ratio of three, maximum debt to cash flow ratio of 3.25 and a minimum net worth of \$180 million plus 50% of consolidated net income since September 30, 2003. The Company is in compliance with these measurements and covenants.

### *6<sup>7</sup>/8% Senior Notes Due August 2013*

In August 2003, the Company issued \$150 million of Senior Notes due in 2013 (the "Notes"). The Notes were issued at par. Interest on the notes accrues at a rate of 6.875% per annum and is payable semi-annually on January 31 and July 31 of each year. The proceeds were used to repay debt outstanding under the Company's existing credit agreement, and for general corporate purposes.

The Company believes, based on current levels of operations and forecasted earnings, cash flow and liquidity will be sufficient to fund its working capital and capital equipment needs as well as to meet its debt service requirements. If the Company's sources of funds were to fail to satisfy the Company's cash requirements, the Company may need to refinance its existing debt or obtain additional financing. There is no assurance that such new financing alternatives would be available, and, in any case, such new financing, if available, would be expected to be more costly and burdensome than the debt agreements currently in place.

On July 31, 2006, the Board of Directors authorized the repurchase of up to \$50 million of the Company's outstanding shares. The Company intends to purchase these shares on the open market or in negotiated or block trades. No time limit was set for the completion of the program which qualifies under the Refinancing Credit Agreement, as well as the 6<sup>7</sup>/8% Senior Notes currently outstanding.

## **Forward Looking Statements**

We believe that all statements other than statements of historical facts included in this report, including certain statements under "Business" and "Management's Discussion and Analysis of Financial Condition and Results of Operations," may constitute forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. Although we believe that our assumptions made in connection with the forward-looking statements are reasonable, we cannot assure you that our assumptions and expectations are correct.

These forward-looking statements are subject to various risks, uncertainties and assumptions about us, including, among other things:

Economic and industry conditions

materially adverse changes in economic or industry conditions generally or in the markets served by us, including North America, South America, Europe, Australia and Asia;

demand for freight cars, locomotives, passenger transit cars, buses and related products and services;

reliance on major original equipment manufacturer customers;

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original equipment manufacturers program delays;

demand for services in the freight and passenger rail industry;

demand for our products and services;

orders either being delayed, cancelled, not returning to historical levels, or reduced or any combination of the foregoing;

consolidations in the rail industry;

continued outsourcing by our customers; industry demand for faster and more efficient braking equipment; or

fluctuations in interest rates and foreign currency exchange rates;

Operating factors

supply disruptions;

technical difficulties;

changes in operating conditions and costs;

increases in raw material costs;

successful introduction of new products;

performance under material long-term contracts;

labor relations;

completion and integration of acquisitions; or

the development and use of new technology;

Competitive factors

the actions of competitors;  
Political/governmental factors

political stability in relevant areas of the world;

future regulation/deregulation of our customers and/or the rail industry;

levels of governmental funding on transit projects, including for some of our customers;

political developments and laws and regulations; or

the outcome of our existing or any future legal proceedings, including litigation involving our principal customers and any litigation with respect to environmental, asbestos-related matters and pension liabilities; and  
Transaction or commercial factors

the outcome of negotiations with partners, governments, suppliers, customers or others.  
Statements in this 10-Q apply only as of the date on which such statements are made, and we undertake no obligation to update any statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

#### **Critical Accounting Policies**

The preparation of the financial statements in accordance with generally accepted accounting principles requires management to make judgments, estimates and assumptions regarding uncertainties that affect the

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reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Areas of uncertainty that require judgments, estimates and assumptions include the accounting for derivatives, environmental matters, warranty reserves, the testing of goodwill and other intangibles for impairment, proceeds on assets to be sold, pensions and other postretirement benefits, and tax matters. Management uses historical experience and all available information to make these judgments and estimates, and actual results will inevitably differ from those estimates and assumptions that are used to prepare the Company's financial statements at any given time. Despite these inherent limitations, management believes that Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) and the financial statements and related footnotes provide a meaningful and fair perspective of the Company. A discussion of the judgments and uncertainties associated with accounting for derivatives and environmental matters can be found in the Notes to Consolidated Financial Statements included elsewhere in this report.

On January 1, 2006, Wabtec adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment, which requires the company to recognize compensation expense for stock-based compensation based on the fair value of the share-based employee grants. SFAS No. 123(R) revises SFAS No. 123 Accounting for Stock-Based Compensation and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees. Wabtec elected the modified prospective application method for adoption, and prior periods financial statements have not been restated.

SFAS No. 123(R) requires Wabtec to recognize compensation expense for stock-based compensation ratably over the requisite service period based on the fair value of the grant. Compensation expense for the Employee Stock Purchase Plan, and Non-Vested Stock awards are based on fair market values determined at the date of award. Prior to the adoption of SFAS No. 123(R), the company accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations using the intrinsic value method, which resulted in no compensation cost for options granted.

Stock based compensation was \$6 million and \$625,000 for the six months ended June 30, 2006 and 2005, respectively. The primary reason for the increase in stock based compensation expense between years is the issuance of shares in 2006 under a non-vested stock plan and increased expense under a stock based incentive plan as a result of the improved performance of the Company. The accounting for the non-vested stock and the stock awards under the incentive plan was not impacted significantly by the adoption of FAS 123(R). In addition, compensation expense of \$593,000 was recorded for the six months ended June 30, 2006 related to the expensing of stock options in accordance with FAS 123(R).

The Company uses a Black-Scholes pricing model to estimate the fair value of stock options at grant date. Determining the fair value of stock options at grant date requires judgment, including estimates for the dividend yield, the average risk-free interest rate, expected volatility and expected life. The dividend yield is based on the Company's dividend rate and the current market price of the underlying common stock. The risk-free interest rate is based on the U.S. Treasury bond rate for the expected life of the option. Expected life in years is determined from historical stock option exercise data. Expected volatility is based on the historical volatility of Wabtec stock. If any of these assumptions differ significantly from actual, stock-based compensation expense could be impacted.

Stock awards under the incentive plans vest upon the achievement of certain financial goals for each three year period ending at December 31, 2006, 2007 and 2008, respectively. We estimate that the majority of stock awards granted will vest and have recorded compensation expense accordingly. If our estimate of the number of these stock awards expected to vest changes in a future accounting period, compensation expense could be reduced and will be recognized over the remaining vesting period.

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A summary of the Company's significant accounting policies is included in Note 2 in the Notes to Consolidated Financial Statements included elsewhere in this report. Management believes that the application of these policies on a consistent basis enables the Company to provide the users of the financial statements with useful and reliable information about the Company's operating results and financial condition.

Description <b>Accounts Receivable and Allowance for Doubtful Accounts:</b>	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
The Company provides an allowance for doubtful accounts to cover anticipated losses on uncollectible accounts receivable.	The allowance for doubtful accounts receivable reflects our best estimate of probable losses inherent in our receivable portfolio determined on the basis of historical experience, specific allowances for known troubled accounts and other currently available evidence.	If our estimates regarding the collectibility of troubled accounts, and/or our actual losses within our receivable portfolio exceed our historical experience, we may be exposed to the expense of increasing our allowance for doubtful accounts.
<b>Inventories:</b>		
Inventories are stated at the lower of cost or market.	Cost is determined under the first-in, first-out (FIFO) method. Inventory costs include material, labor and overhead.	If the market value of our products were to decrease due to changing market conditions, the Company could be at risk of incurring the cost of additional reserves to adjust inventory value to a market value lower than stated cost.

Inventory is reviewed to ensure that an adequate provision is recognized for excess, slow moving and obsolete inventories.

The Company compares inventory components to prior year sales history and current backlog and anticipated future requirements. To the extent that inventory parts exceed estimated usage and demand, a reserve is recognized to reduce the carrying value of inventory. Also, specific reserves are established for known inventory obsolescence.

If our estimates regarding sales and backlog requirements are inaccurate, we may be exposed to the expense of increasing our reserves for slow moving and obsolete inventory.

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Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
<b>Goodwill and Indefinite-Lived Intangibles:</b>		
Goodwill and indefinite-lived intangibles are required to be tested for impairment at least annually. The evaluation of impairment involves comparing the current fair value of the business to the recorded value (including goodwill).	We use a combination of a guideline public company market approach and a discounted cash flow model ( DCF model ) to determine the current fair value of the business. A number of significant assumptions and estimates are involved in the application of the DCF model to forecast operating cash flows, including markets and market share, sales volume and pricing, costs to produce and working capital changes.	Management considers historical experience and all available information at the time the fair values of its business are estimated. However, actual amounts realized may differ from those used to evaluate the impairment of goodwill.
		If actual results are not consistent with our assumptions and judgments used in estimating future cash flows and asset fair values, we may be exposed to additional impairment losses that could be material to our results of operations.
<b>Warranty Reserves:</b>		
The Company provides warranty reserves to cover expected costs from repairing or replacing products with durability, quality or workmanship issues occurring during established warranty periods.	In general, reserves are provided for as a percentage of sales, based on historical experience. In addition, specific reserves are established for known warranty issues and their estimable losses.	If actual results are not consistent with the assumptions and judgments used to calculate our warranty liability, the Company may be at risk of realizing

material gains or losses.

**Accounting for Pensions and Postretirement Benefits:**

These amounts are determined using actuarial methodologies and incorporate significant assumptions, including the rate used to discount the future estimated liability, the long-term rate of return on plan assets and several assumptions relating to the employee workforce (salary increases, medical costs, retirement age and mortality).

Significant judgments and estimates are used in determining the liabilities and expenses for pensions and other postretirement benefits.

The rate used to discount future estimated liabilities is determined considering the rates available at year-end on debt instruments that could be used to settle the obligations of the plan. The long-term rate of return is estimated by considering historical returns and expected returns on current and projected asset allocations and is generally applied to a five-year average market value of assets.

If assumptions used in determining the pension and other postretirement benefits change significantly, these costs can fluctuate materially from period to period.



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	Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
<b>Income Taxes:</b>	As a global company, Wabtec records an estimated liability or benefit for income and other taxes based on what it determines will likely be paid in various tax jurisdictions in which it operates.	The estimate of our tax obligations are uncertain because management must use judgment to estimate the exposures associated with our various filing positions.	Management uses its best judgment in the determination of these amounts. However, the liabilities ultimately realized and paid are dependent on various matters including the resolution of the tax audits in the various affected tax jurisdictions and may differ from the amounts recorded.
<b>Revenue Recognition:</b>	Revenue is recognized in accordance with Staff Accounting Bulletins (SABs) 101, Revenue Recognition in Financial Statements and 104 Revision of Topic 13.	Revenue is recognized when products have been shipped to the respective customers, title has passed and the price for the product has been determined.	An adjustment to the estimated liability would be recorded through income in the period in which it becomes probable that the amount of the actual liability differs from the recorded amount.  Should market conditions and customer demands dictate changes to our standard shipping terms, the Company may be impacted by

The Company recognizes revenues on long-term contracts based on the percentage of completion method of accounting. The units-of-delivery method or other measures, as appropriate, are used to measure the progress toward completion of individual contracts. Contract revenues and cost estimates are reviewed and revised at a minimum quarterly and adjustments are reflected in the accounting period as such amounts are determined.

Certain pre-production costs relating to long term production and supply contracts have been deferred and will be recognized over the life of the contracts.

For long-term contracts, revenues and cost estimates are reviewed and revised at a minimum quarterly and adjustments are reflected in the accounting period as such amounts are determined.

Pre-production costs are recognized over the expected life of the contract usually based on the Company's progress toward the estimated number of units expected to be delivered under the production or supply contract.

longer than typical revenue recognition cycles.

Provisions are made currently for estimated losses on uncompleted contracts.

A charge to expense for unrecognized portions of pre-production costs could be realized if the Company's estimate of the number of units to be delivered changes or the underlying contract is cancelled.

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### **Recent Accounting Pronouncements**

See Notes 2 and 6 of Notes to Condensed Consolidated Financial Statements included elsewhere in this report.

### **Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

#### **Interest Rate Risk**

In the ordinary course of business, Wabtec is exposed to risks that increases in interest rates may adversely affect funding costs associated with its variable-rate debt. There was no outstanding variable-rate debt at June 30, 2006.

#### **Foreign Currency Exchange Risk**

The Company occasionally enters into several types of financial instruments for the purpose of managing its exposure to foreign currency exchange rate fluctuations in countries in which the Company has significant operations. As of June 30, 2006, we had several such instruments outstanding to hedge currency rate fluctuation in 2006.

The Company entered into foreign currency forward contracts to reduce the impact of changes in currency exchange rates. Forward contracts are agreements with a counterparty to exchange two distinct currencies at a set exchange rate for delivery on a set date at some point in the future. There is no exchange of funds until the delivery date. At the delivery date we can either take delivery of the currency or settle on a net basis. All outstanding forward contracts and option agreements are for the sale of U.S. Dollars (USD) and the purchase of Canadian Dollars (CAD). As of June 30, 2006, the Company has forward contracts with a notional value of \$30.0 million CAD (or \$25.2 million U.S.), with an average exchange rate of \$0.84 USD per \$1 CAD, resulting in the recording of a current asset and an increase in comprehensive income of \$1.1 million, net of tax.

Wabtec is also subject to certain risks associated with changes in foreign currency exchange rates to the extent its operations are conducted in currencies other than the U.S. dollar. For the first six months of 2006, approximately 67% of Wabtec's net sales are in the United States, 12% in Canada, 2% in Mexico, and 19% in other international locations, primarily Europe.

### **Item 4. CONTROLS AND PROCEDURES**

Wabtec's principal executive officer and its principal financial officer have evaluated the effectiveness of Wabtec's disclosure controls and procedures, (as defined in Exchange Act Rule 13a-15(e)) as of June 30, 2006. Based upon their evaluation, the principal executive officer and principal financial officer concluded that Wabtec's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by Wabtec in the reports filed or submitted by it under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to provide reasonable assurance that information required to be disclosed by Wabtec in such reports is accumulated and communicated to Wabtec's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

There was no change in Wabtec's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2006, that has materially affected, or is reasonably likely to materially affect, Wabtec's internal control over financial reporting.

**Table of Contents****PART II OTHER INFORMATION****Item 1. LEGAL PROCEEDINGS AND COMMITMENTS AND CONTINGENCIES**

Except as disclosed in Note 12 of the Company's Notes to Condensed Consolidated Financial Statements for the Quarterly Period Ended June 30, 2006, there have been no other material changes to report regarding the Company's commitments and contingencies as described in Note 18 of the Company's Annual Report on Form 10-K for the Year Ended December 31, 2005.

**Item 1A. RISK FACTORS**

There have been no material changes in our risk factors from those disclosed in our 2005 Annual Report on Form 10-K.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

The Annual Meeting of Stockholders of the Company was held May 19, 2006. Three matters were considered and voted upon at the Annual Meeting: the election of three persons to serve as directors, approval of the Amended and Restated Stock Incentive Plan, and approval of the Amended and Restated Director Plan.

**Election of Directors** Nominations of Kim G. Davis, Michael W.D. Howell, and Gary C. Valade, to serve as directors for a term expiring in 2009 were considered and each nominee was elected. All three are independent and are not employees of the Company.

The voting was as follows:

Nominee	Title	Votes For	Votes Against	Votes Withheld
Kim G. Davis	Managing Director of Charlesbank Capital Partners, LLC	42,188,428		763,033
Michael W. D. Howell	Chief Executive Officer of Transport Initiatives Edinburgh Limited	40,927,223		2,024,238
Gary C. Valade	Director	40,783,640		2,167,821

Robert J. Brooks, Emilio A. Fernandez, Lee B. Foster II, William E. Kassling, James V. Napier and Albert J. Neupaver will serve as directors until their terms expire and until their successors have been duly elected and qualified.

**Approval of the Amended and Restated Stock Incentive Plan and Amended and Restated Director Plan** On February 16, 2006, the Board approved amendments to and amended and restated the stock incentive plan (the Amended and Restated Stock Incentive Plan) to replace the 2000 Stock Incentive Plan. Also on February 16, 2006, the Board approved the amendments to and amended and restated the director plan (the Amended and Restated Director Plan) to replace the 1995 Nonemployee Directors' Fee and Stock Option Plan.

The voting was as follows:

Approval for Amendments to	Votes For	Votes Against	Abstain	Votes Withheld
Amended and Restated Stock Incentive Plan	33,544,412	4,772,576	34,279	4,600,194
Amended and Restated Director Plan	36,219,491	1,828,315	303,462	4,600,193

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**Item 6. EXHIBITS**

The following exhibits are being filed with this report:

- 3.1 Restated Certificate of Incorporation of the Company dated January 30, 1995, as amended March 30, 1995, filed as an exhibit to the Company's Registration Statement on Form S-1 (No. 33-90866), and incorporated herein by reference.
- 3.2 Amended and Restated By-Laws of the Company, dated as of January 6, 2006, filed as an exhibit to Form 8-K filed on January 9, 2006.
- 31.1 Rule 13a-14(a) Certification of Chief Executive Officer
- 31.2 Rule 13a-14(a) Certification of Chief Financial Officer
- 32.1 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WESTINGHOUSE AIR BRAKE

TECHNOLOGIES CORPORATION

By: */s/* ALVARO GARCIA-TUNON  
**Alvaro Garcia-Tunon,**

**Senior Vice President,**

**Chief Financial Officer and Secretary**

DATE: August 7, 2006

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**EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Description and Method of Filing</b>
3.1	Restated Certificate of Incorporation of the Company dated January 30, 1995, as amended March 30, 1995, filed as an exhibit to the Company's Registration Statement on Form S-1 (No. 33-90866), and incorporated herein by reference.
3.2	Amended and Restated By-Laws of the Company, dated as of January 6, 2006, filed as an exhibit to Form 8-K filed on January 9, 2006.
31.1	Rule 13a-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer and Chief Financial Officer