

ASTRONICS CORP  
Form 10-Q/A  
March 14, 2007

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**Form 10-Q/A**  
**Amendment No. 1**

**Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
**For the quarterly period ended July 1, 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 0-7087**

**ASTRONICS CORPORATION**

(Exact name of registrant as specified in its charter)

**New York**

(State or other jurisdiction of  
incorporation or organization)

**16-0959303**

(IRS Employer Identification Number)

**130 Commerce Way East Aurora, New York**

(Address of principal executive offices)

**14052**

(Zip code)

**(716) 805-1599**

(Registrant's telephone number, including area code)

**NOT APPLICABLE**

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

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

**\$.01 par value Common Stock, \$.01 par value Class B Stock**

(Title of Class)

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, 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

As of July 1, 2006 7,942,344 shares of common stock were outstanding consisting of 6,499,364 shares of common stock (\$.01 par value) and 1,442,981 shares of Class B common stock (\$.01 par value).

**EXPLANATORY NOTE**

We have restated the Company's unaudited consolidated financial statements for the three and six months ended July 1, 2006 in this Amendment No. 1 on Form 10-Q/A ( Form 10-Q/A ) to our Quarterly Report on Form 10-Q for the Quarter Ended July 1, 2006 (the Form 10-Q ) initially filed with the Securities and Exchange Commission (the Commission ) on August 11, 2006 (the Original Filing ). This, which reflects second quarter 2006 restated financial statements and related footnote disclosures to correct an error which overstated sales reported on the income statement for the three months ended July 1, 2006 by \$0.2 million and understated sales reported on the income statement for the six months ended July 1, 2006 by \$0.1 million. There was no restatement necessary for the three and six months ended July 2, 2005.

As required by Rule 12b-15 promulgated under the Securities and Exchange Act of 1934, Astronic's principal executive officer and principal financial officer are providing Rule 13a-14(a) certifications dated March 14, 2007 in connection with this Form 10-K/A (but otherwise identical to their prior certifications) and are also furnishing, but not filing, written statements pursuant to section 906 of the Sarbanes-Oxley Act of 2002 dated March 14, 2007 (but otherwise identical to their prior statements); and Astronics is re-filing the Consent of Independent Registered Public Accounting Firm dated March 14, 2007 (identical to the previously filed consent).

The amendment on Form 10-K/A ( Form 10-K/A ) to the Company's Annual Report on Form 10-K for the period ended December 31, 2005, initially filed with the Securities and Exchange Commission on March 27, 2006 (the Original Filing ), reflects 2005 restated financial statements and related footnote disclosures to correct an error which overstated sales reported on the income statement at December 31, 2005 by \$1.0 million and net income by \$0.4 million.

On March 5, 2007, the Company concluded that its financial statements for the year ended December 31, 2005 and each of the quarters ended April 1, 2006, July 1, 2006 and September 30, 2006 should be restated to correct an error whereby the Company incorrectly reported revenue from a bill and hold arrangement with one customer.

This correction resulted in the following:

| (In thousands)   | Six Months Ended |              | Three months ended |              | December 31, 2005 |
|--|------------------|--------------|--------------------|--------------|-------------------|
|  | July 1, 2006     | July 1, 2005 | July 1, 2006       | July 2, 2005 |                   |
| a) An increase (reduction) in Sales  | \$ 130           | \$           | \$ (207)           | \$           | N/A               |
| b) An increase (reduction) in Cost of Products Sold associated with the reduction in Sales                                 | 45               |              | (129)              |              | N/A               |
| c) An increase (reduction) in Income Before Taxes from Continuing Operations   | 85               |              | (78)               |              | N/A               |
| d) An increase (reduction) Income Tax Expense associated with the change in Income Before Taxes from Continuing Operations | 29               |              | (26)               |              | N/A               |
| e) An increase (reduction) in Net Income   | 56               |              | (52)               |              | N/A               |
| f) No change in Basic Earnings Per Share   |                  |              |                    |              | N/A               |
| g) An increase (reduction) in Diluted Earnings Per Share   | 0.01             |              | (0.01)             |              | N/A               |
| h) An increase in Deferred Revenue due to the related change in Sales  | 868              |              | 868                |              | \$ 998            |
| i) An increase in Finished Goods Inventory due to the related change in Cost of Products Sold                              | 323              |              | 323                |              | 368               |

| (In thousands)  | Six Months Ended |                 | Three months ended |                 | December<br>31, 2005 |
|---|------------------|-----------------|--------------------|-----------------|----------------------|
|   | July 1,<br>2006  | July 1,<br>2005 | July 1,<br>2006    | July 2,<br>2005 |                      |
| j) An increase in Current Deferred tax Assets associated with the reduction in Income Before Taxes from Continuing Operations | 185              |                 | 185                |                 | 214                  |
| k) A reduction in Retained Earnings associated with the correction  | (360)            |                 | (360)              |                 | (416)                |

All referenced amounts in this report as of July 1, 2006 and December 31, 2005 and for the three and six months ended July 1, 2006, reflect balances and amounts on a restated basis. All of our future Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q and Form 10Q/A will reflect the restated information included in this Form 10-Q/A, as applicable. There were no restatements for the three and six months ended July 2, 2005.

This Form 10-Q/A is filed as part of the restatement (the Restatement ) of our previously issued financial statements for the year ended December 31, 2005 as well as the Company's selected financial data for 2005 as set forth in Item 6 of the Company's Annual Report on Form 10-K for the year ended December 31, 2005. Accordingly, we are also filing with the Commission substantially contemporaneously herewith (i) an amendment on Form 10-K/A to our Annual Report on Form 10-K for the year ended December 31, 2005, (ii) an amendment on Form 10-Q/A to our Quarterly Report on Form 10-Q for the quarter ended April 1, 2006 and (iii) an amendment on Form 10-Q/A to our Quarterly Report on Form 10-Q for the quarter ended September 30, 2006.

These additional amended filings with the Commission correct the same types of errors noted above. We do not intend to file any other amended Annual Reports on Form 10-K affected by this Restatement.

This Amendment No. 1 amends only the following portions of the 10-Q; the remainder of the form 10-Q is unchanged and is not reproduced in the Amendment No. 1. The Amendment No. 1 does not reflect the events occurring after the original filing date of the Form 10-Q. Also, the Original Filing has been amended to contain currently dated certifications from the Company's Chief Executive Officer and Chief Financial Officer, as required by Sections 302 and 906 of the Sarbanes-Oxley Act (See Exhibits 31.1, 31.2 and 32).

This Amendment No. 1 contains changes to the following disclosures:

Part I, Item 1 Financial Statements

Part I, Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations

Part I, Item 4 Controls and Procedures

Part II, Item 6 Exhibits and reports on Form 8-K

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**PART I FINANCIAL INFORMATION****Item 1. Financial Statements**

## ASTRONICS CORPORATION

**Consolidated Balance Sheet**

July 1, 2006

With Comparative Figures for December 31, 2005

(dollars in thousands)

|  | July 1,<br>2006<br>Restated<br>(Unaudited) | December<br>31,<br>2005<br>Restated |
|--|--|-------------------------------------|
| Current Assets:  |  |                                     |
| Cash and Cash Equivalents  | \$ 425                                     | \$ 4,473                            |
| Accounts Receivable, net of allowance for doubtful accounts of \$311 in 2006 and \$365 in 2005 | 17,784                                     | 12,635                              |
| Inventories  | 23,546                                     | 19,381                              |
| Prepaid Expenses   | 1,022                                      | 626                                 |
| Deferred Taxes   | 1,058                                      | 989                                 |
| <br>Total Current Assets   | <br>43,835                                 | <br>38,104                          |
| Property, Plant and Equipment, at cost   | 33,322                                     | 31,665                              |
| Less Accumulated Depreciation and Amortization   | 12,237                                     | 11,204                              |
| <br>Net Property, Plant and Equipment  | <br>21,085                                 | <br>20,461                          |
| Intangible Assets, net of accumulated amortization of \$483 in 2006 and \$329 in 2005          | 3,246                                      | 3,400                               |
| Goodwill   | 2,761                                      | 2,686                               |
| Other Assets   | 1,750                                      | 1,788                               |
| <br>Total Assets   | <br>\$ 72,677                              | <br>\$ 66,439                       |

See notes to financial statements.

ASTRONICS CORPORATION  
**Consolidated Balance Sheet**

July 1, 2006

With Comparative Figures for December 31, 2005  
(dollars in thousands)

|   | July 1,<br>2006<br>Restated<br>(Unaudited) | December<br>31,<br>2005<br>Restated |
|---|--|-------------------------------------|
| <b>Current Liabilities:</b>   |  |                                     |
| Current Maturities of Long-term Debt  | \$ 919                                     | \$ 914                              |
| Note Payable  | 6,000                                      | 7,000                               |
| Accounts Payable  | 10,167                                     | 5,421                               |
| Accrued Payroll and Employee Benefits   | 3,653                                      | 3,861                               |
| Income Taxes Payable  | 219  | 171                                 |
| Customer Advanced Payments and Deferred Revenue   | 4,969                                      | 5,402                               |
| Contract Loss Reserve   |  | 830                                 |
| Other Accrued Expenses  | 1,256                                      | 1,156                               |
| <b>Total Current Liabilities</b>  | <b>27,183</b>                              | <b>24,755</b>                       |
| <br>  |  |                                     |
| Long-term Debt  | 9,868                                      | 10,304                              |
| Supplemental Retirement Plan and Other Benefits   | 4,579                                      | 4,494                               |
| Other Liabilities   | 1,337                                      | 1,317                               |
| Deferred Income Taxes   | 210  | 151                                 |
| <br>  |  |                                     |
| <b>Shareholders' Equity:</b>  |  |                                     |
| Common Stock, \$.01 par value Authorized 20,000,000 shares, issued 7,177,801 in 2006, 7,082,100 in 2005 | 72   | 71                                  |
| Class B Stock, \$.01 par value Authorized 5,000,000 shares, issued 1,548,793 in 2006, 1,603,323 in 2005 | 15   | 16                                  |
| Additional Paid-in Capital  | 4,533                                      | 3,808                               |
| Accumulated Other Comprehensive Income  | 875  | 799                                 |
| Retained Earnings   | 27,724                                     | 24,443                              |
|   | 33,219                                     | 29,137                              |
| <br>  |  |                                     |
| Less Treasury Stock: 784,250 shares in 2006 and 2005  | 3,719                                      | 3,719                               |
| <br>  |  |                                     |
| <b>Total Shareholders' Equity</b>   | <b>29,500</b>                              | <b>25,418</b>                       |
| <br>  |  |                                     |
| <b>Total Liabilities and Shareholders' Equity</b>   | <b>\$ 72,677</b>                           | <b>\$ 66,439</b>                    |

See notes to financial statements.

ASTRONICS CORPORATION  
**Consolidated Statement of Income and Retained Earnings**

Six Months Ended July 1, 2006  
 With Comparative Figures for 2005  
 (Unaudited)  
 (dollars in thousands except per share data)

|  | Six Months Ended            |                 | Three Months Ended          |                 |
|--|-----------------------------|-----------------|-----------------------------|-----------------|
|  | July 1,<br>2006<br>Restated | July 2,<br>2005 | July 1,<br>2006<br>Restated | July 2,<br>2005 |
| Sales  | \$ 54,095                   | \$ 34,495       | \$ 28,832                   | \$ 18,839       |
| Costs and Expenses:                          |                             |                 |                             |                 |
| Cost of products sold                        | 41,917                      | 27,707          | 22,066                      | 15,344          |
| Selling, general and administrative expenses | 6,462                       | 4,793           | 3,443                       | 2,582           |
| Interest expense, net of interest income     | 418                         | 317             | 219                         | 191             |
| Other (income) expense                       | (34)                        | (4)             | (22)                        |                 |
| Total costs and expenses                     | 48,763                      | 32,813          | 25,706                      | 18,117          |
| Income Before Income Taxes                   | 5,332                       | 1,682           | 3,126                       | 722             |
| Provision for Income Taxes                   | 2,051                       | 876             | 1,163                       | 525             |
| Net Income                                   | \$ 3,281                    | \$ 806          | \$ 1,963                    | \$ 197          |
| Retained Earnings:                           |                             |                 |                             |                 |
| Beginning of period                          | 24,443                      | 22,206          |                             |                 |
| End of period                                | \$ 27,724                   | \$ 23,012       |                             |                 |
| Earnings per share:                          |                             |                 |                             |                 |
| Basic  | \$ 0.41                     | \$ 0.10         | \$ 0.25                     | \$ 0.02         |
| Diluted                                      | \$ 0.40                     | \$ 0.10         | \$ 0.24                     | \$ 0.02         |

See notes to financial statements



ASTRONICS CORPORATION  
**Consolidated Statement of Cash Flows**  
Six Months Ended July 1, 2006  
With Comparative Figures for 2005  
(Unaudited)

| (dollars in thousands)   | July 1,<br>2006<br>Restated | July 2,<br>2005 |
|--|-----------------------------|-----------------|
| <b>Cash Flows from Operating Activities:</b>   |                             |                 |
| Net income   | \$ 3,281                    | \$ 806          |
| Adjustments to reconcile net income to cash (used in) provided by operating activities:        |                             |                 |
| Depreciation and Amortization  | 1,259                       | 1,322           |
| Deferred Taxes   | (13)                        | 527             |
| Other  | (46)                        | (89)            |
| Provision for Doubtful Accounts  | (21)                        |                 |
| Stock Compensation Expense   | 329                         |                 |
| Cash flows from changes in operating assets and liabilities, excluding effects of acquisition: |                             |                 |
| Accounts Receivable  | (5,062)                     | (3,126)         |
| Inventories  | (4,094)                     | (2,775)         |
| Prepaid Expenses   | (409)                       | 39              |
| Accounts Payable   | 4,718                       | 2,684           |
| Accrued Expenses   | (81)                        | 640             |
| Customer Advanced Payments and Deferred Revenue  | (433)                       |                 |
| Contract Loss Reserves   | (830)                       |                 |
| Income Taxes   | 49                          | 114             |
| Supplemental Retirement and Other Liabilities  | 84                          |                 |
| Cash (used in) provided by Operating Activities  | (1,269)                     | 142             |
| <b>Cash Flows from Investing Activities:</b>   |                             |                 |
| Business Acquisition   |                             | (13,366)        |
| Proceeds from sale of short-term investments   |                             | 1,000           |
| Capital Expenditures   | (1,607)                     | (1,333)         |
| Other  |                             | (142)           |
| Cash used in Investing Activities  | (1,607)                     | (13,841)        |
| <b>Cash Flows from Financing Activities:</b>   |                             |                 |
| Principal Payments on Long-term Debt and Capital Lease Obligations                             | (483)                       | (467)           |
| Proceeds from Note Payable   |                             | 7,000           |
| Payment on Note Payable  | (1,000)                     |                 |
| Proceeds from exercise of stock options  | 324                         | 162             |
| Income tax benefit from exercise of stock options  | 72                          |                 |
| Cash (used in) provided by Financing Activities  | (1,087)                     | 6,695           |

|   |         |          |
|---|---------|----------|
| Effect of Exchange Rates on Cash                          | (85)    | 44       |
| Cash used in Continuing Operations                        | (4,048) | (6,960)  |
| Cash used in Discontinued Operations operating activities |         | (423)    |
| Net decrease in Cash and Cash Equivalents                 | (4,048) | (7,383)  |
| Cash at Beginning of Period                               | 4,473   | 8,476    |
| Cash at End of Period                                     | \$ 425  | \$ 1,093 |

See notes to financial statements

ASTRONICS CORPORATION  
**Notes to Consolidated Financial Statements**

July 1, 2006  
(Unaudited)

**1) Basis of Presentation**

The accompanying unaudited statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of results for the full year. Operating results for the six month period ended July 1, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

The balance sheet at December 31, 2005 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

For further information, refer to the financial statements and footnotes thereto included in Astronics Corporation's (the Company) 2005 annual report on Form 10-K/A for the year ended December 31, 2005.

**2) Stock Based Compensation**

The Company has stock option plans that authorize the issuance of options for shares of Common Stock to directors, officers and key employees. Stock option grants are designed to reward long-term contributions to the Company and provide incentives for recipients to remain with the Company. The exercise price, determined by a committee of the Board of Directors, may not be less than the fair market value of the Common Stock on the grant date. Options become exercisable over periods not exceeding ten years. The Company's practice has been to issue new shares upon the exercise of the options.

During the first quarter of 2006, the Company adopted SFAS 123(R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the statement of earnings based on the grant date fair value of the award. Under the modified prospective method, the Company is required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The Company uses a straight-line method of attributing the value of stock-based compensation expense, subject to minimum levels of expense, based on vesting. Stock compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Vesting requirements vary for directors, officers and key employees. In general, options granted to outside directors vest six months from the date of grant and options granted to officers and key employees straight line vest over a five-year period from the date of grant.

The fair value of stock options granted was estimated on the date of grant using the Black-Scholes option-pricing model. The weighted average fair value of the options was \$6.05 for options granted during the six months ended July 1, 2006 and was \$3.32 for options granted during the six months ended July 2, 2005. The following table provides the range of assumptions used to value stock options granted during the six months ended July 1, 2006 and July 2, 2005.

|                          | Six Months Ended |              |
|--------------------------|------------------|--------------|
|                          | July 1,<br>2006  | July 2, 2005 |
| Expected volatility      | 0.34             | 0.33         |
| Risk-free rate           | 4.70%            | 5.34%        |
| Expected dividends       | 0.00%            | 0.00%        |
| Expected term (in years) | 7 Years          | 7 10 Years   |



To determine expected volatility, the Company uses historical volatility based on weekly closing prices of its Common Stock and considers currently available information to determine if future volatility is expected to differ over the expected terms of the options granted. The risk-free rate is based on the United States Treasury yield curve at the time of grant for the appropriate term of the options granted. Expected dividends are based on the Company's history and expectation of dividend payouts. The expected term of stock options is based on vesting schedules, expected exercise patterns and contractual terms.

The table below reflects net earnings and net earnings per share for the three and six months ended July 1, 2006 compared with the pro forma information for the three and six months ended July 2, 2005 as follows:

|  | Six Months Ended |                 | Three Months Ended |                 |
|--|------------------|-----------------|--------------------|-----------------|
|  | July 1,<br>2006  | July 2,<br>2005 | July 1,<br>2006    | July 2,<br>2005 |
| (in thousands, except per share data)                                | Restated         |                 | Restated           |                 |
| Net earnings, as reported for the prior period (1)                   | \$ N/A           | \$ 806          | \$ N/A             | \$ 197          |
| Stock compensation expense   | 329              | 208             | 187                | 116             |
| Tax benefit  | (51)             | (75)            | (35)               | (42)            |
| Stock compensation expense, net of tax (2)                           | 278              | 133             | 152                | 74              |
| Net earnings, including the effect of stock compensation expense (3) | \$ 3,281         | \$ 673          | \$ 1,963           | \$ 123          |
| Net earnings per share:  |                  |                 |                    |                 |
| Basic, as reported for the prior period (1)                          | \$ N/A           | \$ .10          | \$ N/A             | \$ .02          |
| Basic, including the effect of stock compensation expense (3)        | \$ .41           | \$ .09          | \$ .25             | \$ .02          |
| Diluted, as reported for the prior period (1)                        | \$ N/A           | \$ .10          | \$ N/A             | \$ .02          |
| Diluted, including the effect of stock compensation expense (3)      | \$ .40           | \$ .08          | \$ .24             | \$ .02          |

(1) Net earnings and earnings per share prior to 2006 did not include stock compensation expense for stock options.

(2) Stock compensation expense prior to 2006 is calculated based on the pro forma application of SFAS No. 123.

- (3) Net earnings and earnings per share prior to 2006 represents pro forma information based on SFAS 123.

A summary of the Company's stock option activity and related information for the six months ended July 1, 2006 is as follows:

| (in thousands, except per option data) | Number<br>of<br>Options | 2006<br>Weighted<br>Average<br>Exercise Price<br>per option | Aggregate<br>Intrinsic<br>Value |
|--|-------------------------|---|---------------------------------|
| Outstanding at December 31, 2005       | 801,583                 | \$ 6.49   | \$ 5,522                        |
| Options Granted                        | 25,000                  | 13.41   | (1)                             |
| Options Exercised                      | (44,846)                | 8.13  | (236)                           |
| Outstanding at July 1, 2006            | 781,737                 | 6.62  | 5,285                           |
| Exercisable at July 1, 2006            | 472,688                 | \$ 6.12   | \$ 3,432                        |

The aggregate intrinsic value in the preceding table represents the total pretax option holder's intrinsic value, based on the Company's closing stock price of Common Stock of \$13.38 as of July 1, 2006, which would have been received by the option holders had all option holders exercised their options as of that date.

The fair value of options vested since December 31, 2005 is \$0.2 million. At July 1, 2006, total compensation costs related to non vested awards not yet recognized amounts to \$0.9 million and will be recognized over a weighted average period of 2.1 years.

The following is a summary of weighted average exercise prices and contractual lives for outstanding and exercisable stock options as of July 1, 2006:

| Exercise Price Range | Shares  | Outstanding<br>Weighted<br>Average<br>Remaining<br>Life<br>in Years | Weighted<br>Average<br>Exercise<br>Price | Shares  | Exercisable<br>Weighted<br>Average<br>Remaining<br>Life<br>in Years | Weighted<br>Average<br>Exercise<br>Price |
|----------------------|---------|---|--|---------|---|--|
| \$2.59-\$4.60        | 59,195  | 1.1   | \$ 3.90                                  | 59,195  | 1.1   | \$ 3.90                                  |
| \$5.09- \$7.65       | 550,639 | 7.0   | \$ 5.62                                  | 348,995 | 6.4   | \$ 5.63                                  |
| \$9.83 - \$13.49     | 171,903 | 7.4   | \$10.73                                  | 64,498  | 4.0   | \$ 10.83                                 |
|                      | 781,737 | 6.6   | \$ 6.62                                  | 472,688 | 5.4   | \$ 6.12                                  |

### **3) Acquisition**

On February 3, 2005, the Company acquired substantially all of the assets of the General Dynamics - Airborne Electronic Systems (AES) business unit from a subsidiary of General Dynamics. Astronics AES produces a wide range of products related to electrical power generation, in-flight control, and distribution on military, commercial, and business aircraft. On the acquisition date, the Company paid \$13.0 million in cash and incurred approximately \$0.4 million in acquisition costs. The Company borrowed \$7.0 million on its credit facility and used \$6.4 million of cash on hand to finance the purchase and acquisition costs. Results of operations include the results of Astronics AES since February 3, 2005, the date of the acquisition.

The following table summarizes the gross carrying amount and accumulated amortization for major categories of acquired intangible assets:

| (in thousands)                         | Weighted<br>Average<br>Life | Gross<br>Carrying<br>Amount<br>July 1,<br>2006 | Accumulated<br>Amortization<br>July 1,<br>2006 | Gross<br>Carrying<br>Amount<br>Dec. 31,<br>2005 | Accumulated<br>Amortization<br>Dec 31,<br>2005 |
|--|-----------------------------|--|--|---|--|
| Patents                                | 12<br>Years                 | \$ 1,271                                       | \$ 140   | \$ 1,271  | \$ 91  |
| Trade Names                            | N/A                         | 553  |  | 553   |  |
| Completed and unpatented<br>technology | 10<br>Years                 | 487  | 69   | 487   | 45   |
| Government contracts                   | 6<br>Years                  | 347  | 82   | 347   | 53   |
| Backlog                                | 4<br>Years                  | 314  | 192  | 314   | 140  |
| Total Intangible assets                |                             | \$ 2,972                                       | \$ 483   | \$ 2,972  | \$ 329   |

Amortization expense for each of the next five years is expected to amount to \$0.3 million for the year ended December 31, 2006 and \$0.2 million for each of the years ended December 31, 2007, 2008, 2009 and 2010.

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The following summary, prepared on a pro forma basis, combines the consolidated results of operations of the Company with those of the acquired business as if the acquisition took place on January 1, 2005. The pro forma consolidated results include the impact of adjustments, including depreciation, amortization of intangibles, increased interest expense on acquisition debt and related income tax effects.

| Unaudited<br><br>(in thousands, except for per share data) | Six Months Ended |              | Three Months Ended |              |
|--|------------------|--------------|--------------------|--------------|
|  | July 2, 2005     | July 2, 2005 | July 2, 2005       | July 2, 2005 |
|  | As<br>Reported   | Pro Forma    | As<br>Reported     | Pro Forma    |
| Sales  | \$34,495         | \$36,194     | \$18,840           | \$18,840     |
| Net income   | 806              | 598          | 197                | 197          |
| Basic earnings per share                                   | 0.10             | 0.08         | 0.02               | 0.02         |
| Diluted earnings per share                                 | 0.10             | 0.08         | 0.02               | 0.02         |

The pro forma results are not necessarily indicative of what would have actually occurred if the acquisition had taken place on January 1, 2005. In addition, they are not intended to be a projection of future results.



**4) Discontinued Operations**

In December of 2002 the Company announced the discontinuance of the Electroluminescent Lamp Business Group, whose business has involved sales of microencapsulated electroluminescent lamps to customers in the consumer electronics industry. The liabilities of discontinued operations at July 2, 2005 consisted of lease payments for equipment that was used in this business, the remaining payments under these leases were made during 2005. As of December 31, 2005 there were no remaining assets or liabilities of discontinued operations.

**5) Inventories**

Inventories are stated at the lower of cost or market, cost being determined in accordance with the first-in, first-out method. Inventories are as follows:

| (in thousands)   | July 1,<br>2006<br>Restated | December<br>31,<br>2005<br>Restated |
|------------------|-----------------------------|-------------------------------------|
| Finished Goods   | \$ 3,124                    | \$ 3,026                            |
| Work in Progress | 10,576                      | 7,805                               |
| Raw Material     | 9,846                       | 8,550                               |
|                  | \$ 23,546                   | \$ 19,381                           |

**6) Comprehensive Income and Accumulated Other Comprehensive Income**

The components of comprehensive income are as follows:

| (in thousands)                           | Six Months Ended            |                 | Three Months Ended          |                 |
|--|-----------------------------|-----------------|-----------------------------|-----------------|
|  | July 1,<br>2006<br>Restated | July 2,<br>2005 | July 1,<br>2006<br>Restated | July 2,<br>2005 |
| Net income                               | \$ 3,281                    | \$ 806          | \$ 1,963                    | \$ 197          |
| Other comprehensive income:              |                             |                 |                             |                 |
| Foreign currency translation adjustments | 71                          | (79)            | 88                          | (10)            |
| Gain on derivatives, net of tax          | 5                           | 37              | 22                          | 15              |
| Comprehensive income                     | \$ 3,357                    | \$ 764          | \$ 2,073                    | \$ 202          |

The components of accumulated other comprehensive income are as follows:

| (in thousands)                              | July 1,<br>2006 | December<br>31,<br>2005 |
|---|-----------------|-------------------------|
| Cumulative foreign currency adjustments     | \$ 870          | \$ 799                  |
| Accumulated gain on derivatives, net of tax | 5               | 0                       |
| Accumulated other comprehensive income      | \$ 875          | \$ 799                  |



**7) Earnings Per Share**

The following table sets forth the computation of earnings per share:

| (in thousands, except per share data)              | Six Months Ended |                 | Three Months Ended |                 |
|--|------------------|-----------------|--------------------|-----------------|
|  | July 1,<br>2006  | July 2,<br>2005 | July 1,<br>2006    | July 2,<br>2005 |
|  | Restated         |                 | Restated           |                 |
| Net Income   | \$ 3,281         | \$ 806          | \$ 1,963           | \$ 197          |
| Basic earnings per share weighted average shares   | 7,925            | 7,835           | 7,937              | 7,857           |
| Net effect of dilutive stock options               | 258              | 127             | 286                | 166             |
| Diluted earnings per share weighted average shares | 8,183            | 7,962           | 8,223              | 8,023           |
| Basic earnings per share                           | \$ 0.41          | \$ 0.10         | \$ 0.25            | \$ 0.02         |
| Diluted earnings per share                         | \$ 0.40          | \$ 0.10         | \$ 0.24            | \$ 0.02         |

**8) Supplemental Retirement Plan and Related Post Retirement Benefits**

The Company has a non-qualified supplemental retirement defined benefit plan for certain executives. The following table sets forth information regarding the net periodic pension cost for the plan.

| (in thousands)                       | Six Months Ended |                 | Three Months Ended |                 |
|--------------------------------------|------------------|-----------------|--------------------|-----------------|
|                                      | July 1,<br>2006  | July 2,<br>2005 | July 1,<br>2006    | July 2,<br>2005 |
| Service cost                         | \$ 18            | \$ 12           | \$ 9               | \$ 6            |
| Interest cost                        | 154              | 154             | 77                 | 77              |
| Amortization of prior service cost   | 54               | 54              | 27                 | 27              |
| Amortization of net actuarial losses | 2                |                 | 1                  |                 |
| Net periodic cost                    | \$ 228           | \$ 220          | \$ 114             | \$ 110          |

Participants in the non-qualified supplemental retirement plan are entitled to paid medical, dental and long-term care insurance benefits upon retirement under the plan. The following table sets forth information regarding the net periodic cost recognized for those benefits:

| (in thousands)                       | Six Months Ended |                 | Three Months Ended |                 |
|--------------------------------------|------------------|-----------------|--------------------|-----------------|
|                                      | July 1,<br>2006  | July 2,<br>2005 | July 1,<br>2006    | July 2,<br>2005 |
| Service cost                         | \$ 4             | \$ 2            | \$ 2               | \$ 1            |
| Interest cost                        | 22               | 20              | 11                 | 10              |
| Amortization of prior service cost   | 16               | 16              | 8                  | 8               |
| Amortization of net actuarial losses | 6                | 2               | 3                  | 1               |
| Net periodic cost                    | \$ 48            | \$ 40           | \$ 24              | \$ 20           |

**9) New Accounting Pronouncements**

In June 2006, the FASB issued Interpretation ( FIN ) No. 48, Accounting for Uncertainty in Income Taxes an Interpretation for SFAS No. 109. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with for SFAS No. 109, Accounting for Income Taxes. The pronouncement prescribes a recognition threshold and measurement attributable to financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. We are in the process of determining the effect, if any; the adoption of FIN 48 will have on our financial statements.

**10) Income Taxes**

On April 12, 2005, New York State enacted tax legislation resulting in a change to the New York State apportionment methodology. Beginning in 2006, a single sales factor apportionment method will be phased in, with a single sales factor solely used in 2008. It is expected that this enacted legislation will result in a lower apportionment of the Company's taxable income to New York State, resulting in lower New York state income taxes. Accordingly, the Company's ability to use or realize New York State tax credits has been reduced. In 2005, the Company has assessed the impact of the new tax legislation and recorded a valuation allowance reducing the Company's \$490 thousand deferred tax asset relating to New York State tax credits to \$40 thousand. As a result of this valuation allowance the Company recorded a non-cash charge to income tax expense of \$300 thousand or \$0.04 per diluted share during the second quarter of 2005. The charge to income tax expense is net of the affect of federal income taxes. The effective tax rate in 2006 returned to a more normal rate of 38.5%

**11) Restatement of Previously Issued Financial Statements**

The Company has restated its previously issued financial statements for the year ended December 31, 2005, the three months ended April 1, 2006 and the three and six months ended July 1, 2006 to correct an error regarding the timing of revenue recognition for a bill-and-hold transaction. This error reduces revenue previously reported on the income statement for the year ended December 31, 2005 by \$1.0 million and net income by \$0.4 million. This error understated sales reported on the income statement for the six months ended July 1, 2006 by \$0.1 million and understated net income by \$0.1 million. This error overstated sales reported on the income statement for the three months ended July 1, 2006 by \$0.2 million and overstated net income by \$0.1 million. There were no changes necessary to the quarterly financial statements and information for the comparative period ended July 2, 2005. This correction resulted in the following:

| (In thousands) |   | Six Months Ended |                 | Three months ended |                 | December |
|----------------|---|------------------|-----------------|--------------------|-----------------|----------|
|                |   | July 1,<br>2006  | July 1,<br>2005 | July 1,<br>2006    | July 2,<br>2005 | 31, 2005 |
| a)             | An increase (reduction) in Sales  | \$ 130           | \$              | \$ (207)           | \$              | N/A      |
| b)             | An increase (reduction) in Cost of Products Sold associated with the reduction in Sales                                 | 45               |                 | (129)              |                 | N/A      |
| c)             | An increase (reduction) in Income Before Taxes from Continuing Operations   | 85               |                 | (78)               |                 | N/A      |
| d)             | An increase (reduction) Income Tax Expense associated with the change in Income Before Taxes from Continuing Operations | 29               |                 | (26)               |                 | N/A      |
| e)             | An increase (reduction) in Net Income   | 56               |                 | (52)               |                 | N/A      |
| f)             | No change in Basic Earnings Per Share   |                  |                 |                    |                 | N/A      |
| g)             | An increase (reduction) in Diluted Earnings Per Share   | 0.01             |                 | (0.01)             |                 | N/A      |
| h)             | An increase in Deferred Revenue due to the related change in Sales  | 868              |                 | 868                |                 | \$ 998   |

|    |  |       |       |       |
|----|--|-------|-------|-------|
| i) | An increase in Finished Goods Inventory due to the related change in Cost of Products Sold                                 | 323   | 323   | 368   |
| j) | An increase in Current Deferred tax Assets associated with the reduction in Income Before Taxes from Continuing Operations | 185   | 185   | 214   |
| k) | A reduction in Retained Earnings associated with the correction  | (360) | (360) | (416) |
|    |  | 14    |       |       |

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**CONSOLIDATED BALANCE SHEET**

| <i>(in thousands, except per share data)</i>                                 | As<br>Reported | July 1, 2006<br>Adjustments | As<br>Restated |
|--|----------------|-----------------------------|----------------|
| Current Assets:  |                |                             |                |
| Cash and Cash Equivalents  | \$ 425         | \$                          | \$ 425         |
| Accounts Receivable, net of allowance for doubtful accounts of \$311 in 2006 | 17,784         |                             | 17,784         |
| Inventories  | 23,223         | 323                         | 23,546         |
| Prepaid Expenses   | 1,022          |                             | 1,022          |
| Deferred Taxes   | 873            | 185                         | 1,058          |
| Total Current Assets   | 43,327         | 508                         | 43,835         |
| Property, Plant and Equipment, at cost                                       | 33,322         |                             | 33,322         |
| Less Accumulated Depreciation and Amortization                               | 12,237         |                             | 12,237         |
| Net Property, Plant and Equipment  | 21,085         |                             | 21,085         |
| Intangible Assets, net of accumulated amortization of \$483 in 2006          | 3,246          |                             | 3,246          |
| Goodwill   | 2,761          |                             | 2,761          |
| Other Assets   | 1,750          |                             | 1,750          |
| Total Assets   | \$72,169       | \$ 508                      | \$72,677       |

**CONSOLIDATED BALANCE SHEET** (continued)

| <i>(in thousands, except per share data)</i>  | July 1, 2006    |               |                 |
|---|-----------------|---------------|-----------------|
|   | As<br>Reported  | Adjustments   | As<br>Restated  |
| <b>Current Liabilities:</b>   |                 |               |                 |
| Current Maturities of Long-term Debt  | \$ 919          | \$            | \$ 919          |
| Note Payable  | 6,000           |               | 6,000           |
| Accounts Payable  | 10,167          |               | 10,167          |
| Accrued Payroll and Employee Benefits   | 3,653           |               | 3,653           |
| Income Taxes Payable  | 219             |               | 219             |
| Customer Advanced Payments and Deferred Revenue   | 4,101           | 868           | 4,969           |
| Contract Loss Reserve   |                 |               |                 |
| Other Accrued Expenses  | 1,256           |               | 1,256           |
| <b>Total Current Liabilities</b>  | <b>26,315</b>   | <b>868</b>    | <b>27,183</b>   |
| <br>  |                 |               |                 |
| Long-term Debt  | 9,868           |               | 9,868           |
| Supplemental Retirement Plan and Other Benefits   | 4,579           |               | 4,579           |
| Other Liabilities   | 1,337           |               | 1,337           |
| Deferred Income Taxes   | 210             |               | 210             |
| <b>Shareholders' Equity:</b>  |                 |               |                 |
| Common Stock, \$.01 par value Authorized 20,000,000 shares,<br>issued 7,177,801 in 2006 | 72              |               | 72              |
| Class B Stock, \$.01 par value Authorized 5,000,000 shares, issued<br>1,548,793 in 2006 | 15              |               | 15              |
| Additional Paid-in Capital  | 4,533           |               | 4,533           |
| Accumulated Other Comprehensive Income  | 875             |               | 875             |
| Retained Earnings   | 28,084          | (360)         | 27,724          |
|   | 33,579          | (360)         | 33,219          |
| Less Treasury Stock: 784,250 shares in 2006   | 3,719           |               | 3,719           |
| <b>Total Shareholders' Equity</b>   | <b>29,860</b>   | <b>(360)</b>  | <b>29,500</b>   |
| <br>  |                 |               |                 |
| <b>Total Liabilities and Shareholders' Equity</b>                                       | <b>\$72,169</b> | <b>\$ 508</b> | <b>\$72,677</b> |



**CONSOLIDATED BALANCE SHEET**

| <i>(in thousands, except per share data)</i>                                 | December 31, 2005 |             |             |
|--|-------------------|-------------|-------------|
|  | As Reported       | Adjustments | As Restated |
| Current Assets:  |                   |             |             |
| Cash and Cash Equivalents  | \$ 4,473          | \$          | \$ 4,473    |
| Accounts Receivable, net of allowance for doubtful accounts of \$365 in 2005 | 12,635            |             | 12,635      |
| Inventories  | 19,013            | 368         | 19,381      |
| Prepaid Expenses   | 626               |             | 626         |
| Deferred Taxes   | 775               | 214         | 989         |
| Total Current Assets   | 37,522            | 582         | 38,104      |
| Property, Plant and Equipment, at cost                                       | 31,665            |             | 31,665      |
| Less Accumulated Depreciation and Amortization                               | 11,204            |             | 11,204      |
| Net Property, Plant and Equipment  | 20,461            |             | 20,461      |
| Intangible Assets, net of accumulated amortization of \$329 in 2005          | 3,400             |             | 3,400       |
| Goodwill   | 2,686             |             | 2,686       |
| Other Assets   | 1,788             |             | 1,788       |
| Total Assets   | \$65,857          | \$ 582      | \$66,439    |

**CONSOLIDATED BALANCE SHEET** (continued)

| <i>(in thousands, except per share data)</i>  | December 31, 2005 |               |                 |
|---|-------------------|---------------|-----------------|
|   | As<br>Reported    | Adjustments   | As<br>Restated  |
| <b>Current Liabilities:</b>   |                   |               |                 |
| Current Maturities of Long-term Debt  | \$ 914            | \$            | \$ 914          |
| Note Payable  | 7,000             |               | 7,000           |
| Accounts Payable  | 5,421             |               | 5,421           |
| Accrued Payroll and Employee Benefits   | 3,861             |               | 3,861           |
| Income Taxes Payable  | 171               |               | 171             |
| Customer Advanced Payments and Deferred Revenue   | 4,404             | 998           | 5,402           |
| Contract Loss Reserve   | 830               |               | 830             |
| Other Accrued Expenses  | 1,156             |               | 1,156           |
| <b>Total Current Liabilities</b>  | <b>23,757</b>     | <b>998</b>    | <b>24,755</b>   |
| <br>  |                   |               |                 |
| Long-term Debt  | 10,304            |               | 10,304          |
| Supplemental Retirement Plan and Other Benefits   | 4,494             |               | 4,494           |
| Other Liabilities   | 1,317             |               | 1,317           |
| Deferred Income Taxes   | 151               |               | 151             |
| <br>  |                   |               |                 |
| <b>Shareholders' Equity:</b>  |                   |               |                 |
| Common Stock, \$.01 par value Authorized 20,000,000 shares,<br>issued 7,082,100 in 2005 | 71                |               | 71              |
| Class B Stock, \$.01 par value Authorized 5,000,000 shares, issued<br>1,603,323 in 2005 | 16                |               | 16              |
| Additional Paid-in Capital  | 3,808             |               | 3,808           |
| Accumulated Other Comprehensive Income  | 799               |               | 799             |
| Retained Earnings   | 24,859            | (416)         | 24,443          |
|   | 29,553            | (416)         | 29,137          |
| Less Treasury Stock: 784,250 shares in 2005   | 3,719             |               | 3,719           |
| <b>Total Shareholders' Equity</b>   | <b>25,834</b>     | <b>(416)</b>  | <b>25,418</b>   |
| <br>  |                   |               |                 |
| <b>Total Liabilities and Shareholders' Equity</b>                                       | <b>\$65,857</b>   | <b>\$ 582</b> | <b>\$66,439</b> |

**CONSOLIDATED STATEMENT OF OPERATIONS**

| <i>(in thousands, except per share data)</i>            | Six Months Ended July 1, 2006 |             |             | Three Months Ended July 1, 2006 |             |             |
|---|-------------------------------|-------------|-------------|---------------------------------|-------------|-------------|
|   | As Reported                   | Adjustments | As Restated | As Reported                     | Adjustments | As Restated |
| Sales   | \$53,965                      | \$ 130      | \$54,095    | \$29,039                        | \$ (207)    | \$28,832    |
| Costs and Expenses:                                     |                               |             |             |                                 |             |             |
| Cost of products sold                                   | 41,872                        | 45          | 41,917      | 22,195                          | (129)       | 22,066      |
| Selling, general and administrative expenses            | 6,462                         |             | 6,462       | 3,443                           |             | 3,443       |
| Interest expense, net of interest income of \$4 in 2006 | 418                           |             | 418         | 219                             |             | 219         |
| Other (income) expense                                  | (34)                          |             | (34)        | (22)                            |             | (22)        |
| Total costs and expenses                                | 48,718                        | 45          | 48,763      | 25,835                          | (129)       | 25,706      |
| Income Before Income Taxes                              | 5,247                         | 85          | 5,332       | 3,204                           | (78)        | 3,126       |
| Provision for Income Taxes                              | 2,022                         | 29          | 2,051       | 1,189                           | (26)        | 1,163       |
| Net Income  | 3,225                         | 56          | 3,281       | \$ 2,015                        | \$ (52)     | \$ 1,963    |
| Retained Earnings:                                      |                               |             |             |                                 |             |             |
| Beginning of period                                     | 24,859                        | (416)       | 24,443      |                                 |             |             |
| End of period   | \$28,084                      | \$ (360)    | \$27,724    |                                 |             |             |
| Earnings per share:                                     |                               |             |             |                                 |             |             |
| Basic   | \$ .41                        | \$ 0.00     | \$ 0.41     | \$ .25                          | \$ 0.00     | \$ 0.25     |
| Diluted   | .39                           | 0.01        | 0.40        | .25                             | (0.01)      | 0.24        |

**CONSOLIDATED STATEMENT OF CASH FLOWS**

| <i>(in thousands)</i>  | As<br>Reported | July 1, 2006<br>Adjustments | As<br>Restated |
|--|----------------|-----------------------------|----------------|
| <b>Cash Flows from Operating Activities:</b>   |                |                             |                |
| Net income   | \$ 3,225       | \$ 56                       | \$ 3,281       |
| Adjustments to reconcile net income to cash (used in) provided by operating activities:        |                |                             |                |
| Depreciation and Amortization  | 1,259          |                             | 1,259          |
| Deferred Tax Provision   | (42)           | 29                          | (13)           |
| Other  | (46)           |                             | (46)           |
| Provision for Doubtful Accounts  | (21)           |                             | (21)           |
| Stock Compensation Expense   | 329            |                             | 329            |
| Cash flows from changes in operating assets and liabilities, excluding effects of acquisition: |                |                             |                |
| Accounts Receivable  | (5,062)        |                             | (5,062)        |
| Inventories  | (4,139)        | 45                          | (4,094)        |
| Prepaid Expenses   | (409)          |                             | (409)          |
| Accounts Payable   | 4,718          |                             | 4,718          |
| Accrued Expenses   | (81)           |                             | (81)           |
| Customer Advanced Payments and Deferred Revenue  | (303)          | (130)                       | (433)          |
| Contract Loss Reserves   | (830)          |                             | (830)          |
| Income Taxes   | 49             |                             | 49             |
| Supplemental Retirement and Other Liabilities  | 84             |                             | 84             |
| Cash used in Operating Activities  | (1,269)        |                             | (1,269)        |
| <b>Cash Flows from Investing Activities:</b>   |                |                             |                |
| Business Acquisition   |                |                             |                |
| Proceeds from sale of short-term investments   |                |                             |                |
| Capital Expenditures   | (1,607)        |                             | (1,607)        |
| Other  |                |                             |                |
| Cash used in Investing Activities  | (1,607)        |                             | (1,607)        |
| <b>Cash Flows from Financing Activities:</b>   |                |                             |                |
| Principal Payments on Long-term Debt and Capital Lease Obligations                             | (483)          |                             | (483)          |
| Proceeds from Note Payable   |                |                             |                |
| Payment on Note Payable  | (1,000)        |                             | (1,000)        |
| Proceeds from Issuance of Stock  | 324            |                             | 324            |
| Income tax benefit from exercise of stock options  | 72             |                             | 72             |
| Cash used in Financing Activities  | (1,087)        |                             | (1,087)        |

|  |         |    |         |
|--|---------|----|---------|
| Effect of Exchange Rates on Cash                             | (85)    |    | (85)    |
| Cash used in Continuing Operations                           | (4,048) |    | (4,048) |
| Cash used in Discontinued Operations    operating activities |         |    |         |
| Net decrease in Cash and Cash Equivalents                    | (4,048) |    | (4,048) |
| Cash at Beginning of Period                                  | 4,473   |    | 4,473   |
| Cash at End of Period  | \$ 425  | \$ | \$ 425  |

**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (RESTATED)**

(The following should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's Form 10-K/A for the year ended December 31, 2005.)

The following table sets forth income statement data as a percent of net sales:

| (in thousands)  | Six Months Ended            |                 | Three Months Ended          |                 |
|---|-----------------------------|-----------------|-----------------------------|-----------------|
|   | July 1,<br>2006<br>Restated | July 2,<br>2005 | July 1,<br>2006<br>Restated | July 2,<br>2005 |
| Sales   | 100.0%                      | 100.0%          | 100.0%                      | 100.0%          |
| Cost of products sold                                 | 77.5                        | 80.3            | 76.6                        | 81.5            |
| Selling, general and administrative and other expense | 11.9                        | 13.9            | 11.9                        | 13.7            |
| Interest expense and Other (Income) Expense           | 0.7                         | 0.9             | 0.7                         | 1.0             |
| Total cost and expenses                               | 90.1                        | 95.1            | 89.2                        | 96.2            |
| Income before taxes                                   | 9.9%                        | 4.9%            | 10.8%                       | 3.8%            |

***ACQUISITION***

On February 3, 2005, the Company acquired the assets of the Airborne Electronic Systems (AES) business unit from a subsidiary of General Dynamics, for \$13.0 million. The Company used \$6.0 million of cash and borrowed \$7.0 million against its line of credit to finance the acquisition. No goodwill was recognized as a result of this acquisition. Operating results for this acquisition are included in the consolidated statement of earnings from the acquisition date.

***SALES***

Sales for the second quarter of 2006 increased 53.2% to \$28.8 million compared with \$18.8 million for the same period last year. Sales to the commercial transport market were \$16.7 million, as compared to \$8.4 million for the same period of 2005, an increase of \$8.3 million or 98.8 percent. The sales increase to the commercial transport market was primarily a result of increased volume of cabin electronics products. The volume increase has been driven by increased installations of in-seat power and in-flight entertainment systems utilizing our products. The balance of the increase in commercial transport market sales was due to a broad increased demand for the cabin lighting product line. Sales to the business jet market were \$5.4 million, up \$1.3 million, or 32.9%, compared with sales of \$4.1 million for the same period in 2005. The increase of sales to the business jet market is due primarily to an increase in volume as production of new business jets by the airframe manufacturers increased over last year. Sales to the military market were \$6.5 million as compared to \$6.1 million last year, an increase of \$0.4 million or 6.1%. A \$1.0 million increase in sales for airframe power products driven by shipments for the Tactical Tomahawk and Taurus Missile programs was offset by a \$1.0 million decrease in deliveries for F-16 night vision kits for the Korean Air Force. The balance of the increase for military sales was a result of a general increase in volume.

2006 year to date sales increased 56.8 % to \$54.1 million compared with \$34.5 million for the same period last year. Sales to the commercial transport market were up \$14.9 million, or 102.1% to \$29.5 million compared with the year ago period at \$14.6 million. The increase is due to primarily a result of increased volume of cabin electronics products as the commercial airline market continues to strengthen. The volume increase has been driven by increased installations of in-seat power and in-flight entertainment systems utilizing our products. Sales to the business jet market were \$10.3 million, up \$2.2 million, or 27.5%, compared with \$8.1 million for the same period in 2005. The increase of sales to the business jet market is due primarily to an increase in volume as production of new business jets

by the airframe manufacturers increased over last year. Sales to the military market were \$13.6 million, up from \$11.2 million in the same period of 2005. Shipments for the Tactical Tomahawk and Taurus Missile programs were primarily responsible for a \$2.5 million increase of sales for airframe power products to the military markets. This was partially offset by a \$0.9 million decrease in deliveries for F-16 night vision kits for the Korean Air Force as the Korean program was concluded in 2005. The balance of the increase for military sales was a result of a general increase in volume.

A small portion of the 2006 year to date sales increase is due to the timing of the Astronics Advanced Electronic Systems acquisition. The acquisition date was February 3, 2005, as such the first six months of 2005 contained only twenty one weeks of sales for Astronics Advanced Electronic Systems as compared with twenty six weeks in the first six months of 2006.

**EXPENSES AND MARGINS**

Cost of products sold as a percentage of sales decreased 4.9 percentage points to 76.6% for the second quarter of 2006 as compared to 81.5% for the same period last year. That decrease was primarily a result of the leverage provided by sales volume increases without a corresponding increase to our fixed manufacturing costs.

Year to date costs of products sold decreased by 2.8 percentage points to 77.5 % as compared to 80.3% for the same period last year. That decrease was also a result of the leverage provided by sales volume increases without a corresponding increase to our fixed manufacturing costs. That leverage was partially offset by a \$0.9 million increase in engineering and development costs over the same period last year.

Selling, general and administrative and other (SG&A) expense as a percent of sales was 11.9 % for the second quarter of 2006, a decrease of 1.8 percentage points compared with 13.7% for the same period of 2005. Second quarter 2006 SG&A costs increased \$0.8 million to \$3.4 million as compared to the second quarter of 2005. The increase was primarily due to increased wages and benefits due to increased staffing and compensation related costs and increased costs for audit and other professional services related to Sarbanes-Oxley 404 implementation.

For the first six months of 2006 SG&A as a percentage of sales was 11.9% compared to 13.9% for the same period of 2005. In terms of dollars SG&A costs increased \$1.7 million to \$6.5 million for the first six months of 2006 from \$4.8 million in the first six months of 2005. The increase was due to increased wages and benefits due to increased staffing and compensation related costs and increased costs for audit and other professional services related to Sarbanes-Oxley 404 implementation. Also, a portion of the 2006 year to date SG&A increase is due to the timing of the Astronics Advanced Electronic Systems acquisition. The acquisition date was February 3, 2005, as such the first six months of 2005 contained only twenty one weeks of expenses for Astronics Advanced Electronic Systems as compared with twenty six weeks in the first six months of 2006.

Net interest expense for the second quarter of 2006 and 2005 was \$0.2 million. Net interest expense for the six months of 2006 increased by \$0.1 million from \$0.3 million in 2005 to \$0.4 million due to an increase in interest rates, offset somewhat by the impact of a pay down of \$1.0 million on the note payable during the first half of 2006.

**TAXES**

The effective income tax rate for the second quarter of 2006 was 37.2 % compared to 72.7% last year. The 2005 tax rate was due primarily to the Company's assessment of the impact of the new tax legislation in 2005 and the recording of a valuation allowance reducing the Company's \$0.5 million deferred tax asset relating to New York State tax credits to \$40 thousand. As a result of this valuation allowance the Company recorded a non-cash charge to income tax expense of \$0.3 million or \$.04 per share during the second quarter of 2005.

The 2006 year to date effective income tax rate was 38.5% compared to 52.1% last year. Last year's effective rate was impacted by the valuation allowance discussed in the preceding paragraph.

The Company expects its effective income tax rate to continue to approximate the statutory rates in the future.

**NET INCOME AND EARNINGS PER SHARE**

Net income for the second quarter of 2006 was \$2.0 million or \$0.24 per share diluted, an increase of \$1.8 million from \$0.2 million, or \$0.02 per share diluted in the second quarter of 2005. Net income in the second quarter of 2005 was significantly impacted by recording a valuation allowance for certain deferred tax assets referred to in the previous Taxes section. The earnings per share increase was due to increased net income and was not significantly impacted by a change in shares outstanding.



### **LIQUIDITY**

Cash used by operating activities totaled \$1.3 million during the first six months of 2006, as compared with \$0.1 million of cash provided by operations during the first six months of 2005. The change was due primarily to net income being offset by increased investment in net working capital components. The increase in net working capital components is a function of the increased sales over the past several quarters.

Cash used in investing activities decreased to \$1.6 million in the first six months of 2006, from \$13.8 million used in the first six months of 2005. This was due primarily to last year's \$13.4 million acquisition of Astronics Advanced Electronic Systems, offset partially by proceeds from the sale of short-term investments of \$1.0 million in 2005.

Capital expenditures increased by \$0.3 million to \$1.6 million in 2006 compared to \$1.3 million in 2005.

In the first six months of 2006 the Company used \$1.1 million for financing activities as it paid down \$1.0 million on its revolving credit facility and made principal payments against its long term debt totaling \$0.5 million. This was partially offset by proceeds from the issuance of stock relating to the exercise of stock options totaling \$0.4 million. The Company has a \$15 million demand line of credit facility. Interest on outstanding borrowings bears interest at either LIBOR plus an applicable margin, currently 150 basis points or prime interest rate, at the Company's option. As of July 1, 2006 the Company has \$6.0 million outstanding on the line of credit. The line is subject to annual review and is payable on demand. The line of credit, among other requirements, imposes certain financial performance covenants measured on an annual basis with which the Company anticipates it will be compliant.

The Company believes that cash flow from operations and its available credit facility will be adequate to meet the Company's operational and capital expenditure requirements for 2006.

### **BACKLOG**

The Company's backlog at July 1, 2006 was \$89.8 million compared with \$77.9 million at July 2, 2005.

### **CONTRACTUAL OBLIGATIONS AND COMMITMENTS**

The Company's contractual obligations and commercial commitments have not changed materially from disclosures in the Company's Form 10-K/A for the year ended December 31, 2005.

### **MARKET RISK**

Risk due to fluctuation in interest rates is a function of the Company's floating rate debt obligations, which total approximately \$16.8 million at July 1, 2006. To partially offset this exposure, the Company entered into an interest rate swap in February 2006, on its New York Industrial Revenue Bond which effectively fixes the rate at 3.99% on this \$4.3 million obligation through January 2016. As a result, a change of 1% in interest rates would impact annual net income by less than \$0.1 million.

There have been no material changes in the current year regarding the market risk information for its exposure to currency exchange rates. The Company has limited exposure to fluctuation in Canadian currency exchange rates to the U.S. dollar.

Refer to the Company's Annual Report on Form 10-K/A for the year ended December 31, 2005 for a complete discussion of the Company's market risk.

### **CRITICAL ACCOUNTING POLICIES**

Refer to the Company's annual report on Form 10-K/A for the year ended December 31, 2005 for a complete discussion of the Company's critical accounting policies. Other than the adoption of SFAS 123(R), Share-Based Payments, there have been no significant changes in the current year regarding critical accounting policies.

### **RECENT ACCOUNTING PRONOUNCEMENTS**

During the first quarter of 2006, we adopted SFAS 123(R), Share-Based Payment, applying the modified prospective method. This Statement requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the statement of earnings based on the grant date fair value of the award. Under the modified prospective method, we are required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. We use a straight-line method of attributing the value of stock-based compensation expense, based on vesting. Stock compensation expense was \$0.1 million in the second quarter of 2006 and \$0.3 million year to date, after taxes. No stock compensation expense was recognized prior to 2006.

In November 2004, the FASB issued SFAS No. 151 Inventory Costs, an amendment of ARB No. 43, Chapter 4. The amendments made by this statement clarify that abnormal amounts of idle facility expense, freight, handling costs and wasted materials (spoilage) should be recognized as current-period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The provisions of this statement are effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The adoption of this standard did not have an impact on its results of operations, cash flows or financial position in the first half of 2006.

In June 2006, the FASB issued Interpretation ( FIN ) No. 48, Accounting for Uncertainty in Income Taxes an Interpretation for SFAS No. 109. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with for SFAS No. 109, Accounting for Income Taxes. The pronouncement prescribes a recognition threshold and measurement attributable to financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. The company is in the process of determining the effect, if any; the adoption of FIN 48 will have on our financial statements.

### **FORWARD-LOOKING STATEMENTS**

This Quarterly Report contains certain forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involves uncertainties and risks. These statements are identified by the use of the words believes, expects, intends, anticipates, may, will, estimate, potential and words of similar import cautioned not to place undue reliance on these forward looking statements as various uncertainties and risks could cause actual results to differ materially from those anticipated in these statements. These uncertainties and risks include the success of the Company with effectively executing its plans; the timeliness of product deliveries by vendors and other vendor performance issues; changes in demand for our products from the U.S. government and other customers; the acceptance by the market of new products developed; our success in cross-selling products to different customers and markets; changes in government contracts; the state of the commercial and business jet aerospace market; the Company's success at increasing the content on current and new aircraft platforms; the level of aircraft build rates; as well as other general economic conditions and other factors.

### **Item 4. Controls and Procedures**

As discussed in Note 11 of the Notes to Condensed Consolidated Financial Statements (Restated), contained in Part I, Item 1 of this Form 10-Q/A, we have restated in this Form 10-Q/A our unaudited consolidated financial statements for the three and six months ended July 1, 2006 (the Second Quarter Restatement). This Item 4 has been updated to reflect the Second Quarter Restatement which is related to the correction of an error in our recognition of revenue for a bill and hold relationship with one customer.

#### **Evaluation of Disclosure Controls and Procedures (Restated)**

(a) Disclosure Controls and Procedures: The Company carried out an evaluation, under the supervision and with the participation of Company Management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures are effective as of the end of the period covered by this report, to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is made known to them on a timely basis, and that these disclosure controls and procedures are effective to ensure such

information is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. However, as described below in "Application of Generally Accepted Accounting Principles" during the Company's 2006 year-end audit the Company became aware that its revenue recognition policy with regard to a bill and hold arrangement with one customer did not meet all of the criteria necessary to allow it to recognize revenue for the transaction while the product remained in the Company's facility. As such Management has concluded that a material weakness in the Company's internal control over financial reporting existed at July 1, 2006.

(b) Changes in Internal Control over Financial Reporting: There have been no changes in the Company's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. As such, the material weakness in our internal control over financial reporting that existed as of December 31, 2005, as described and as disclosed in Part II, Item 9A of our Amended 2005 Form 10-K/A, continued to exist as of July 1, 2006.

**Application of Generally Accepted Accounting Principles**

During the Company's 2006 year-end audit the Company became aware that its revenue recognition policy with regard to a bill and hold arrangement with one customer did not meet all of the criteria necessary to allow it to recognize revenue for the transaction while the product remained in the Company's facility. As such Management has concluded that a material weakness in the Company's internal control over financial reporting existed at July 1, 2006. The Company believes it has taken action to remediate the weakness that includes training with regard to bill and hold arrangements and approval of any proposed bill and hold arrangement by the CEO and CFO of the Company.

**PART II OTHER INFORMATION**

**Item 6 Exhibits and Reports on Form 8-K**

**(a) Exhibits**

Exhibit 31.1 Section 302 Certification Chief Executive Officer

Exhibit 31.2 Section 302 Certification Chief Financial Officer

Exhibit 32. Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

**(b) Reports on Form 8-K**

On May 11, 2006, Astronics Corporation issued a news release in Form 8-K announcing its financial results for the first quarter of 2006.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**ASTRONICS CORPORATION**

(Registrant)

Date: March 14,  
2007

By: /s/ David C. Burney

David C. Burney  
Vice President-Finance and Treasurer  
(Principal Financial Officer)

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