

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORP
Form 10-Q
August 09, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2007

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

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

1001 Air Brake Avenue

Wilmerding, PA
(Address of principal executive offices)

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

15148
(Zip Code)

412-825-1000

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(Registrant's telephone number, including area code)

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 7, 2007 |
|---|-------------------------------|
| Common Stock, \$.01 par value per share | 48,758,666 shares |

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**WESTINGHOUSE AIR BRAKE
TECHNOLOGIES CORPORATION**

June 30, 2007 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> | Unaudited June 30, 2007 | December 31, 2006 |
|--|--|------------------------------|
| Assets | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 141,226 | \$ 187,979 |
| Accounts receivable | 201,411 | 177,345 |
| Inventories | 184,605 | 145,481 |
| Deferred income taxes | 23,711 | 24,773 |
| Other current assets | 17,890 | 11,613 |
| Total current assets | 568,843 | 547,191 |
| Property, plant and equipment | 405,407 | 390,178 |
| Accumulated depreciation | (225,763) | (211,869) |
| Property, plant and equipment, net | 179,644 | 178,309 |
| Other Assets | | |
| Goodwill | 224,090 | 173,251 |
| Other intangibles, net | 47,754 | 44,494 |
| Deferred income taxes | 23,847 | 16,588 |
| Other noncurrent assets | 14,411 | 13,009 |
| Total other assets | 310,102 | 247,342 |
| Total Assets | \$ 1,058,589 | \$ 972,842 |
| Liabilities and Shareholders Equity | | |
| Current Liabilities | | |
| Accounts payable | \$ 110,529 | \$ 92,624 |
| Accrued income taxes | 2,080 | 4,491 |
| Customer deposits | 59,134 | 75,537 |
| Accrued compensation | 26,923 | 26,297 |
| Accrued warranty | 10,857 | 10,305 |
| Other accrued liabilities | 34,524 | 34,537 |
| Total current liabilities | 244,047 | 243,791 |
| Long-term debt | 150,000 | 150,000 |
| Reserve for postretirement and pension benefits | 70,410 | 74,511 |
| Deferred income taxes | 15,705 | 15,014 |
| Accrued warranty | 7,781 | 7,094 |
| Other long term liabilities | 29,302 | 12,543 |
| Total liabilities | 517,245 | 502,953 |
| Shareholders Equity | | |

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| | | |
|---|---------------------|-------------------|
| Preferred stock, 1,000,000 shares authorized, no shares issued | | |
| Common stock, \$.01 par value; 100,000,000 shares authorized: 66,174,767 shares issued and 48,730,246 and 48,250,776 outstanding at June 30, 2007 and December 31, 2006, respectively | 662 | 662 |
| Additional paid-in capital | 318,111 | 314,752 |
| Treasury stock, at cost, 17,444,521 and 17,923,991 shares, at June 30, 2007 and December 31, 2006, respectively | (229,246) | (232,823) |
| Retained earnings | 469,578 | 419,603 |
| Accumulated other comprehensive loss | (17,761) | (32,305) |
| Total shareholders equity | 541,344 | 469,889 |
| Total Liabilities and Shareholders Equity | \$ 1,058,589 | \$ 972,842 |

The accompanying notes are an integral part of these statements.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

| <i>In thousands, except per share data</i> | Unaudited | | Unaudited | |
|---|--------------------|------------|------------------|------------|
| | Three Months Ended | | Six Months Ended | |
| | June 30 | | June 30 | |
| | 2007 | 2006 | 2007 | 2006 |
| Net sales | \$ 325,722 | \$ 261,902 | \$ 639,986 | \$ 524,311 |
| Cost of sales | (234,872) | (184,910) | (462,570) | (372,229) |
| Gross profit | 90,850 | 76,992 | 177,416 | 152,082 |
| Selling, general and administrative expense | (34,915) | (32,760) | (69,860) | (66,548) |
| Engineering expense | (9,026) | (8,023) | (17,842) | (16,138) |
| Amortization expense | (1,140) | (852) | (1,828) | (1,711) |
| Total operating expenses | (45,081) | (41,635) | (89,530) | (84,397) |
| Income from operations | 45,769 | 35,357 | 87,886 | 67,685 |
| Other income and expenses | | | | |
| Interest expense, net | (538) | (420) | (1,174) | (1,544) |
| Other expense, net | (1,637) | (1,434) | (2,446) | (1,162) |
| Income from continuing operations before income taxes | 43,594 | 33,503 | 84,266 | 64,979 |
| Income tax expense | (15,469) | (11,721) | (30,587) | (23,129) |
| Income from continuing operations | 28,125 | 21,782 | 53,679 | 41,850 |
| Discontinued operations | | | | |
| Income (loss) from discontinued operations (net of tax) | 5 | (637) | (27) | (659) |
| Net income | \$ 28,130 | \$ 21,145 | \$ 53,652 | \$ 41,191 |
| Earnings Per Common Share | | | | |
| Basic | | | | |
| Income from continuing operations | \$ 0.58 | \$ 0.45 | \$ 1.11 | \$ 0.87 |
| Loss from discontinued operations | | (0.01) | | (0.02) |
| Net income | \$ 0.58 | \$ 0.44 | \$ 1.11 | \$ 0.85 |
| Diluted | | | | |
| Income from continuing operations | \$ 0.57 | \$ 0.44 | \$ 1.09 | \$ 0.86 |
| Loss from discontinued operations | | (0.01) | | (0.02) |
| Net income | \$ 0.57 | \$ 0.43 | \$ 1.09 | \$ 0.84 |
| Weighted average shares outstanding | | | | |
| Basic | 48,666 | 48,451 | 48,413 | 48,210 |
| Diluted | 49,294 | 49,092 | 49,022 | 48,851 |

The accompanying notes are an integral part of these statements.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Unaudited | |
|--|-------------------------|-------------------|
| | Six Months Ended | |
| | June 30, | |
| <i>In thousands</i> | 2007 | 2006 |
| Operating Activities | | |
| Net income | \$ 53,652 | \$ 41,191 |
| Stock-based compensation expense | 4,645 | 5,689 |
| Adjustments to reconcile net income to net cash provided by operations: | | |
| Discontinued operations | 114 | (1,154) |
| Depreciation and amortization | 13,971 | 11,859 |
| Excess income tax benefits from exercise of stock options | (1,402) | (4,215) |
| Changes in operating assets and liabilities | | |
| Accounts receivable | (12,265) | 39,876 |
| Inventories | (22,067) | (30,989) |
| Accounts payable | 7,639 | (12,755) |
| Accrued income taxes | 6,181 | 22,279 |
| Accrued liabilities and customer deposits | (21,379) | (10,977) |
| Other assets and liabilities | (2,866) | 12,401 |
| Net cash provided by operating activities | 26,223 | 73,205 |
| Investing Activities | | |
| Purchase of property, plant and equipment and other | (8,342) | (8,969) |
| Proceeds from disposal of property, plant and equipment | 139 | |
| Acquisitions of business, net of cash acquired | (73,264) | |
| Sale of discontinued operations | | 3,018 |
| Net cash used for investing activities | (81,467) | (5,951) |
| Financing Activities | | |
| Proceeds from the issuance of treasury stock for stock options and other benefit plans | 4,310 | 10,187 |
| Stock repurchase | (3,421) | |
| Excess income tax benefits from exercise of stock options | 1,402 | 4,215 |
| Cash dividends (\$0.01 per share for the six months ended June 30, 2007 and 2006) | (986) | (969) |
| Net cash provided by financing activities | 1,305 | 13,433 |
| Effect of changes in currency exchange rates | 7,186 | 16,855 |
| (Decrease) increase in cash | (46,753) | 97,542 |
| Cash, beginning of year | 187,979 | 141,365 |
| Cash, end of period | \$ 141,226 | \$ 238,907 |

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, 2007 (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 100 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 2007, about 38% of the Company's revenues came from outside the U.S.

2. ACCOUNTING POLICIES

Basis of Presentation The unaudited 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 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, 2006. The December 31, 2006 information has been derived from the Company's December 31, 2006 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 certain long-term contracts based on the percentage of completion method of accounting. The units-of-delivery method or other input-based or output-based 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 \$8.4 million and \$6.5 million at June 30, 2007 and December 31, 2006, respectively.

Use of Estimates The preparation of financial statements in conformity with generally accepted accounting principles 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.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

Stock-Based Compensation The Company recognizes compensation expense for stock-based compensation based on the grant date fair value ratably over the requisite service period following the date of grant.

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 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 the Company can either take delivery of the currency or settle on a net basis. At June 30, 2007, the Company had forward contracts for the sale of U.S. Dollars (USD) and the purchase of Canadian Dollars (CAD) with a notional value of \$24.0 million CAD (or \$21.4 million U.S.), with an average exchange rate of \$0.89 USD per \$1 CAD. The Company has determined that these foreign currency contracts qualify for cash flow hedge accounting which permits the recording of the fair value of the forward contract and corresponding adjustment to other comprehensive income (loss), net of tax on the balance sheet. The adjustment resulted in the recording of a current asset and an increase in comprehensive income of \$756,000, net of tax.

At June 30, 2007, the Company had forward contracts for the sale of USD and the purchase of Euro with a notional value of 2.3 million Euro (or \$3.1 million USD), with an average exchange rate of \$1.32 USD per 1 Euro. These forward contracts are used to hedge the variability in cash flows from the payment of liabilities denominated in currencies other than the USD. The change in fair value of both the forward contracts and the related liabilities are recorded in the income statement. For the quarter ended June 30, 2007, the Company recorded a fair value gain in the amount of \$31,000.

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 intercompany transaction losses recognized as other expense were \$1.3 million for the three months ended June 30, 2007 and 2006 and \$2.1 million and \$930,000 for the six months ended June 30, 2007 and 2006, respectively.

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

| <i>In thousands</i> | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|-----------|------------------------------|-----------|
| | 2007 | 2006 | 2007 | 2006 |
| Net income | \$ 28,130 | \$ 21,145 | \$ 53,652 | \$ 41,191 |
| Foreign currency translation adjustment | 9,937 | 9,928 | 12,963 | 10,220 |
| Unrealized gain on foreign exchange contracts, net of tax | 1,232 | 491 | 1,581 | 223 |
| Total comprehensive income | \$ 39,299 | \$ 31,564 | \$ 68,196 | \$ 51,634 |

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

The components of accumulated other comprehensive loss were:

| <i>In thousands</i> | June 30, 2007 | December 31, 2006 |
|--|--------------------------|------------------------------|
| Foreign currency translation adjustment | \$ 23,991 | \$ 11,028 |
| Unrealized gain (loss) on foreign exchange contracts, net of tax | 756 | (825) |
| Pension and post retirement benefit plan adjustments, net of tax | (42,508) | (42,508) |
| Total accumulated comprehensive loss | \$ (17,761) | \$ (32,305) |

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

Recent Accounting Pronouncements In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements, (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions of this standard apply to other accounting pronouncements that require or permit fair value measurements. SFAS 157 becomes effective for Wabtec on January 1, 2008. Upon adoption, the provisions of SFAS 157 are to be applied prospectively with limited exceptions. The adoption of SFAS 157 is not expected to have a material impact on the Company's consolidated financial statements.

The Company adopted the provisions of Financial Accounting Standards Board Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48) an interpretation of FASB Statement No. 109 on January 1, 2007. The implementation of FIN 48 has resulted in a \$2.7 million reduction to the beginning balance of retained earnings, reported as a change in accounting principle. At the adoption date of January 1, 2007, the liability for income taxes associated with uncertain tax positions was \$13.5 million. If uncertain tax positions are recognized, \$8.0 million would favorably affect the Company's effective tax rate. The Company includes interest and penalties related to uncertain tax positions in income tax expense. As of January 1, 2007, the Company has accrued approximately \$1.7 million of interest and \$1.1 million of penalties related to uncertain tax positions.

As of December 31, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106 and 132(R) (SFAS 158). The Company must adopt the measurement date provisions of SFAS 158 by December 31, 2008.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure eligible items at fair value at specified election dates and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of adopting this Statement; however, the adoption is not expected to have an effect on the Company's results of operations or financial position.

3. ACQUISITIONS AND DISCONTINUED OPERATIONS

On June 11, 2007, the Company acquired 100% of the stock of Ricon Corporation (Ricon), a manufacturer of variety of electro-mechanical wheelchair lifts and ramps and anti-graffiti windows. The purchase price was

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\$73.3 million resulting in preliminary additional goodwill of \$45.1 million. On October 6, 2006, the Company acquired 100% of the stock of Schaefer Equipment, Inc. (Schaefer), a manufacturer of a variety of forged components for body-mounted and truck-mounted braking systems. The purchase price was \$36.7 million, net of cash received, resulting in additional goodwill of \$24.2 million. On December 1, 2006, the Company acquired 100% of the stock of Becorit GmbH (Becorit), a manufacturer of a variety of brake shoes, pads and friction linings for passenger transit cars, freight cars and locomotives, and friction products for industrial markets such as mining and wind power generation. The purchase price was \$51.3 million, net of cash received, resulting in additional goodwill of \$33.2 million.

Due to the timing of the Ricon acquisition, we are still in the process of finalizing the valuation of the acquired assets and liabilities, and therefore the purchase price allocation is preliminary and subject to change once finalized. Operating results have been included in the consolidated statement of operations from the acquisition date forward.

For the Ricon acquisition, the following table summarizes the preliminary estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition:

| <i>In thousands</i> | Ricon June 11, 2007 |
|-----------------------------|------------------------------------|
| Current assets | \$ 29,800 |
| Property, plant & equipment | 2,900 |
| Intangible assets | 9,700 |
| Goodwill | 45,100 |
| Other assets | 1,100 |
| | |
| Total assets acquired | 88,600 |
| Current liabilities | (14,300) |
| Other liabilities | (1,000) |
| | |
| Total liabilities assumed | (15,300) |
| | |
| Net assets acquired | \$ 73,300 |

The following unaudited pro forma financial information presents income statement results as if all these acquisitions described above had occurred on January 1, 2006:

| <i>In thousands</i> | Three Months Ended | | Six Months Ended | |
|----------------------------|--------------------|------------------|------------------|------------------|
| | June 30, 2007 | June 30, 2006 | June 30, 2007 | June 30, 2006 |
| Net sales | \$ 337,219 | \$ 295,028 | \$ 668,025 | \$ 588,182 |
| Gross profit | 94,362 | 88,967 | 185,492 | 174,252 |
| Net income | 28,034 | 25,013 | 52,944 | 46,681 |
| Diluted earnings per share | | | | |
| As Reported | \$ 0.57 | \$ 0.43 | \$ 1.09 | \$ 0.84 |

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Pro forma

0.57

0.51

1.07

0.96

At March 31, 2006, the sale of a non-core product division was completed for approximately \$1.4 million in cash, including a working capital adjustment of approximately \$600,000 which was established with the buyer in the fourth quarter of 2006. The assets sold primarily included transit car interior products and services for

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customers located in Europe. This sale resulted in a loss of approximately \$1.7 million including the working capital adjustment. This adjustment is subject to review through independent arbitration and a ruling is expected sometime in late 2007.

In accordance with SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets, the operating results of businesses that have been classified as discontinued operations for all years presented and are summarized as of December 31, as follows:

| <i>In thousands</i> | Three Months Ended | | Six Months Ended | |
|--|--------------------|----------|------------------|----------|
| | 2007 | 2006 | 2007 | 2006 |
| Net sales | \$ | \$ 3 | \$ | \$ 2,600 |
| Income (loss) before income taxes | 5 | (522) | (27) | (497) |
| Income tax benefit | | (115) | | (162) |
| Income (loss) from discontinued operations | \$ 5 | \$ (637) | \$ (27) | \$ (659) |

4. INVENTORIES

The components of inventory, net of reserves, were:

| <i>In thousands</i> | June 30, 2007 | December 31, 2006 |
|---------------------|------------------|----------------------|
| Raw materials | \$ 75,565 | \$ 51,685 |
| Work-in-process | 71,818 | 64,229 |
| Finished goods | 37,222 | 29,567 |
| Total inventory | \$ 184,605 | \$ 145,481 |

5. RESTRUCTURING AND IMPAIRMENT CHARGES

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 downsized two of its Canadian plants, in Stoney Creek and Wallaceburg, by moving certain products to lower-cost facilities and outsourcing. For the three months ended June 30, 2007, Wabtec recorded charges of \$3.0 million, and for the six months ended June 30, 2007, Wabtec recorded charges of \$4.0 million. In the third quarter of 2006, Wabtec recorded charges of \$6.8 million. Total charges for restructuring and other expenses recorded to date as a result of the approval of this plan has been \$10.8 million. These expenses were comprised of the following components: \$2.9 million for employee severance costs associated with approximately 330 salaried and hourly employees located at our Wallaceburg and Stoney Creek locations; \$4.5 million of pension and postretirement benefit curtailment for those employees; \$2.9 million related to asset impairments for structures, machinery, and equipment; and \$541,000 for goodwill impairment specific to the Wallaceburg facility. As of June 30, 2007, the employees associated with the restructuring program had been terminated. Severance costs are contractual liabilities and payment is dependent on the waiver by or expiration of certain seniority rights of those employees. As of June 30, 2007, \$281,000 of this amount had been paid.

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Additional severance, pension, and asset impairment charges of \$1.1 million were recorded in the first quarter of 2007 related to other Canadian operations. As of June 30, 2007, none of these expenses have been paid.

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In the fourth quarter of 2005 and 2006 and during 2007, the Company recorded restructuring charges of about \$1.3 million relating to consolidating two Australian facilities into one. The total charges consisted of severance costs of \$797,000 for 14 employees, relocation and other costs of \$431,000, and an asset impairment of \$56,000. As of June 30, 2007, all but \$133,000 of the restructuring costs had been paid.

6. INTANGIBLES

Goodwill is \$224.1 million and \$173.3 million at June 30, 2007 and December 31, 2006, respectively.

As of June 30, 2007 and December 31, 2006, the Company's trademarks had a net carrying amount of \$24.4 million and \$24.0 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> | June 30, 2007 | December 31, 2006 |
|--|--------------------------|------------------------------|
| Patents and other, net of accumulated amortization of \$28,804 and \$27,305 | \$ 8,349 | \$ 9,245 |
| Customer relationships, net of accumulated amortization of \$1,234 and \$983 | 15,029 | 11,239 |
| Total | \$ 23,378 | \$ 20,484 |

The weighted average useful lives of patents and customer relationships were 13 years and 20 years, respectively. Amortization expense for intangible assets was \$993,000 and \$1.5 million for the three and six months ended June 30, 2007, and \$669,000 and \$1.3 million for the three and six months ended June 30, 2006.

The change in the carrying amount of goodwill by segment for the six months ended June 30, 2007 is as follows:

| <i>In thousands</i> | Freight Group | Transit Group | Total |
|---|--------------------------|--------------------------|-------------------|
| Balance at December 31, 2006 | \$ 112,991 | \$ 60,260 | \$ 173,251 |
| Adjustment to preliminary purchase allocation | 71 | 3,399 | 3,470 |
| Acquisition | | 45,136 | 45,136 |
| Foreign currency impact | 730 | 1,503 | 2,233 |
| Balance at June 30, 2007 | \$ 113,792 | \$ 110,298 | \$ 224,090 |

7. LONG-TERM DEBT

Long-term debt consisted of the following:

| <i>In thousands</i> | June 30, 2007 | December 31, 2006 |
|---------------------|--------------------------|------------------------------|
|---------------------|--------------------------|------------------------------|

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| | | |
|----------------------|------------|------------|
| 6.875% Senior Notes | \$ 150,000 | \$ 150,000 |
| Total | \$ 150,000 | \$ 150,000 |
| Less current portion | | |
| Long term portion | \$ 150,000 | \$ 150,000 |

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

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. The Company entered into an amendment to its Refinancing Credit Agreement in February 2007 which permits the Company to complete any acquisitions without prior approval of the bank consortium as long as certain financial parameters and ratios are met. At June 30, 2007, the Company had available bank borrowing capacity, net of \$22.9 million of letters of credit, of approximately \$152.1 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, 2007 or during the year ended December 31, 2006.

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.

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 3, 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.

6.875% 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 principal balance is due in full at maturity.

The Notes are senior unsecured obligations of the Company and rank pari passu with all existing and future senior debt and 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.

Table of Contents**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)**

No shares were purchased during the first quarter of 2007. During the second quarter 2007, the Company repurchased 92,700 shares of Wabtec stock at an average price of \$36.87 per share.

8. EMPLOYEE BENEFIT PLANS**Defined Benefit Pension Plans**

The Company sponsors defined benefit pension plans that cover certain U.S., Canadian, German 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> | U.S. | | International | |
|---|--------------------------------|--------|--------------------------------|----------|
| | Three months ended June 30, | | Three months ended June 30, | |
| | 2007 | 2006 | 2007 | 2006 |
| Net periodic benefit cost | | | | |
| Service cost | \$ 88 | \$ 105 | \$ 962 | \$ 980 |
| Interest cost | 671 | 656 | 1,688 | 1,340 |
| Expected return on plan assets | (775) | (737) | (1,873) | (1,432) |
| Net amortization/deferrals | 404 | 380 | 408 | 538 |
| Net periodic benefit cost | \$ 388 | \$ 404 | \$ 1,185 | \$ 1,426 |

Assumptions

| | | | | |
|-----------------------------------|-------|-------|-------|-------|
| Discount rate | 5.80% | 5.50% | 5.11% | 5.07% |
| Expected long-term rate of return | 8.00% | 8.00% | 6.70% | 6.50% |
| Rate of compensation increase | 3.00% | 3.00% | 3.62% | 3.68% |

| <i>In thousands, except percentages</i> | U.S. | | International | |
|---|------------------------------|---------|------------------------------|----------|
| | Six months ended June 30, | | Six months ended June 30, | |
| | 2007 | 2006 | 2007 | 2006 |
| Net periodic benefit cost | | | | |
| Service cost | \$ 176 | \$ 210 | \$ 1,884 | \$ 1,943 |
| Interest cost | 1,343 | 1,312 | 3,314 | 2,655 |
| Expected return on plan assets | (1,550) | (1,475) | (3,675) | (2,837) |
| Net amortization/deferrals | 807 | 760 | 799 | 1,068 |
| Net periodic benefit cost | \$ 776 | \$ 807 | \$ 2,322 | \$ 2,829 |

Assumptions

| | | | | |
|-----------------------------------|-------|-------|-------|-------|
| Discount rate | 5.80% | 5.50% | 5.11% | 5.07% |
| Expected long-term rate of return | 8.00% | 8.00% | 6.70% | 6.50% |
| Rate of compensation increase | 3.00% | 3.00% | 3.62% | 3.68% |

The Company's funding methods are based on governmental requirements and differ from those methods used to recognize pension expense, which is primarily based on the projected unit credit method applied in the accompanying financial statements. The Company expects to

contribute \$5.9 million to the U.S. plan and \$7.8 million to the international plans during 2007.

Table of Contents**WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)****Post Retirement Benefit Plans**

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.

| <i>In thousands, except percentages</i> | U.S. | | International | |
|---|--------------------------------|---------------|--------------------------------|---------------|
| | Three months ended June 30, | | Three months ended June 30, | |
| | 2007 | 2006 | 2007 | 2006 |
| Net periodic benefit cost | | | | |
| Service cost | \$ 59 | \$ 252 | \$ 60 | \$ 73 |
| Interest cost | 527 | 559 | 93 | 98 |
| Net amortization/deferrals | (83) | 182 | 61 | 90 |
| Net periodic benefit cost | \$ 503 | \$ 993 | \$ 214 | \$ 261 |

Assumptions

| | | | | |
|---------------|-------|-------|-------|-------|
| Discount rate | 5.80% | 5.80% | 5.25% | 5.25% |
|---------------|-------|-------|-------|-------|

| <i>In thousands, except percentages</i> | U.S. | | International | |
|---|------------------------------|-----------------|------------------------------|---------------|
| | Six months ended June 30, | | Six months ended June 30, | |
| | 2007 | 2006 | 2007 | 2006 |
| Net periodic benefit cost | | | | |
| Service cost | \$ 117 | \$ 503 | \$ 117 | \$ 145 |
| Interest cost | 1,055 | 1,118 | 181 | 193 |
| Net amortization/deferrals | (166) | 365 | 118 | 178 |
| Net periodic benefit cost | \$ 1,006 | \$ 1,986 | \$ 416 | \$ 516 |

Assumptions

| | | | | |
|---------------|-------|-------|-------|-------|
| Discount rate | 5.80% | 5.80% | 5.25% | 5.25% |
|---------------|-------|-------|-------|-------|

9. STOCK-BASED COMPENSATION

Stock-Based Compensation The Company recognizes compensation expense for stock-based compensation based on the grant date fair value ratably over the requisite service period following the date of grant.

Stock based compensation was \$4.6 million and \$5.7 million for the six months ended June 30, 2007 and 2006, respectively. 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 2006. At June 30, 2007, unamortized compensation expense related to those stock options, non-vested shares and stock awards expected to vest totaled \$14.1 million and will be recognized over a weighted average period of 1.6 years.

Stock Options: 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 10 years from the date of grant. In January and February 2007, Wabtec granted 33,000 stock options

to certain individuals.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

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:

| | Three and Six months ended | |
|-------------------------|-------------------------------|------|
| | June 30, | |
| | 2007 | 2006 |
| Dividend yield | .1% | .3% |
| Risk-free interest rate | 4.7% | 4.3% |
| Stock price volatility | 40.7 | 43.4 |
| 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. The risk-free interest rate is based on the U.S. Treasury bond rates for the expected life of the option. Expected volatility is based on the historical volatility of Wabtec stock. Expected life in years is determined from historical stock option exercise data.

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

| | | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life | Aggregate intrinsic value (in thousands) |
|--|-----------------|---------------------------------------|---|--|
| Beginning of year | January 1, 2007 | \$ 13.52 | | \$ 23,198 |
| Granted | | 30.83 | | 121 |
| Exercised | | 11.78 | | 7,533 |
| Canceled | | 26.31 | | 92 |
| Year to date | June 30, 2007 | \$ 14.42 | 5.4 | \$ 24,222 |
| Exercisable | | \$ 13.28 | 5.3 | \$ 22,116 |
| Weighted average fair value of options granted during 2007 | | \$ 11.16 | | |

Non-Vested Restricted Stock and Incentive Stock Awards: The Company adopted a non-vested stock plan in 2006. In February 2007, the Company issued 121,000 awards to certain individuals. The non-vested stock generally vests over four years from the date of grant. In 2004, the Company established a stock-based incentive plan for eligible employees. The plan provides stock awards which vest upon attainment of certain three year performance targets. The Company issued 238,000 awards to certain individuals in February 2007 with 229,000 awards becoming vested during the first quarter of 2007.

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

| | Non-Vested | Incentive | |
|--------------------------------|------------|-----------|-------------|
| | Restricted | Stock | Weighted |
| | Stock | Awards | Average FMV |
| Outstanding at January 1, 2007 | 197,500 | 701,666 | \$ 23.63 |
| Granted | 121,000 | 238,000 | 33.99 |
| Vested | | (229,000) | 31.06 |
| Canceled | | | |
| Outstanding at June 30, 2007 | 318,500 | 710,666 | \$ 25.59 |

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

Stock awards granted 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, 2007, 2008, and 2009, respectively. The stock awards included in the table above represent the maximum number of shares that may ultimately vest. As of June 30, 2007, based on the Company's performance, we have estimated the most probable amount of these stock awards which 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 different and will be recognized in the current period.

10. INCOME TAXES

The overall effective income tax rate was 35.5% and 36.3% for the three and six months ended June 30, 2007 and 35.0% and 35.6% for the three and six months ended June 30, 2006, respectively. During the second quarter of 2007, the Company recorded a tax benefit of \$1.3 million related to the reversal of a state deferred tax valuation allowance.

The Company adopted the provisions of Financial Accounting Standards Board Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48) an interpretation of FASB Statement No. 109 on January 1, 2007. The implementation of FIN 48 has resulted in a \$2.7 million direct reduction to the beginning balance of retained earnings, reported as a change in accounting principle.

At the adoption date of January 1, 2007, the liability for income taxes associated with uncertain tax positions was \$13.5 million. If uncertain tax positions are recognized, \$8.0 million would favorably affect the Company's effective tax rate. The Company includes interest and penalties related to uncertain tax positions in income tax expense. As of January 1, 2007, the Company has accrued approximately \$1.7 million of interest and \$1.1 million of penalties related to uncertain tax positions. These amounts did not materially change as of June 30, 2007.

With limited exception, the Company is no longer subject to examination by various U.S. and foreign taxing authorities for years before 2002. The Internal Revenue Service (IRS) is currently auditing the tax year ended December 31, 2004. In 2007, certain taxing jurisdictions are prevented by statute from further examination of tax years prior to 2004. The Company does not anticipate a significant change to the total amount of unrecognized tax benefits within the next 12 months.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

11. EARNINGS PER SHARE

The computation of earnings per share is as follows:

| <i>In thousands, except per share</i> | Three Months Ended June 30, | |
|---|--|-------------|
| | 2007 | 2006 |
| Basic earnings per share | | |
| Income from continuing operations applicable to common shareholders | \$ 28,125 | \$ 21,782 |
| Divided by | | |
| Weighted average shares outstanding | 48,666 | 48,451 |
| Basic earnings from continuing operations per share | \$ 0.58 | \$ 0.45 |

Diluted earnings per share

| | | |
|---|-----------|-----------|
| Income from continuing operations applicable to common shareholders | \$ 28,125 | \$ 21,782 |
| Divided by sum of the | | |
| Weighted average shares outstanding | 48,666 | 48,451 |
| Conversion of dilutive stock options and non-vested stock | 628 | 641 |
| Diluted shares outstanding | 49,294 | 49,092 |
| Diluted earnings from continuing operations per share | \$ 0.57 | \$ 0.44 |

| <i>In thousands, except per share</i> | Six Months Ended June 30, | |
|---|--------------------------------------|-------------|
| | 2007 | 2006 |
| Basic earnings per share | | |
| Income from continuing operations applicable to common shareholders | \$ 53,679 | \$ 41,850 |
| Divided by | | |
| Weighted average shares outstanding | 48,413 | 48,210 |
| Basic earnings from continuing operations per share | \$ 1.11 | \$ 0.87 |

Diluted earnings per share

| | | |
|---|-----------|-----------|
| Income from continuing operations applicable to common shareholders | \$ 53,679 | \$ 41,850 |
| Divided by sum of the | | |
| Weighted average shares outstanding | 48,413 | 48,210 |
| Conversion of dilutive stock options and non-vested stock | 609 | 641 |
| Diluted shares outstanding | 49,022 | 48,851 |
| Diluted earnings from continuing operations per share | \$ 1.09 | \$ 0.86 |

12. WARRANTIES

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

| <i>In thousands</i> | Six Months Ended | |
|---|------------------|-----------|
| | June 30, | |
| | 2007 | 2006 |
| Balance at December 31, 2006 and 2005, respectively | \$ 17,399 | \$ 16,158 |
| Warranty provision | 5,329 | 5,376 |
| Acquisition | 1,399 | |
| Warranty claim payments | (5,489) | (3,977) |
| Balance at June 30, 2007 and 2006, respectively | \$ 18,638 | \$ 17,557 |

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

13. 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, 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 two arbitration decisions and a judicial opinion, all of which confirmed Wabtec's position that it did not assume any asbestos liabilities from the former owners of certain Wabtec 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.

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 machine 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.

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

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.

In a presentation provided to Wabtec and Faiveley on August 22, 2006, Bombardier claimed that it has reached a settlement with Amtrak and Knorr related to the suspension of Amtrak's Acela service. Bombardier has alleged that it has incurred damages of approximately \$38 million, and has been assigned the rights to pursue additional claims by Amtrak and Knorr of approximately \$17 million and \$10 million, respectively. Wabtec has contacted Faiveley, asserting that Faiveley is fully responsible for any claims made by Bombardier, including the assigned claims of Amtrak and Knorr.

While Wabtec does not believe that it has any material legal liability with regard to this matter, Management has pursued a commercial resolution with Bombardier that would be mutually beneficial to both parties. As a result of those discussions, the Company believes it has reached a framework for a settlement which provides for Bombardier to receive payments based on certain sales with the Company taking into account historical sales volume. If finalized, this arrangement would be in effect from 2007 to 2009, and would be subject to a maximum amount of \$4.4 million in total assuming the corresponding level of sales were reached. The Company has recorded a provision of \$2.5 million for this potential settlement in the first quarter of 2007 to provide for payments that would be payable based on current sales levels.

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 investigation, and has informed Wabtec's Audit Committee, Board of Directors, and the appropriate authorities.

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, 2006, filed on March 1, 2007. During the first six months of 2007, there were no material changes other than what is discussed above to the information described in Note 18 therein.

14. 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 primarily to the production and operation of freight cars and locomotives, including braking control equipment, on-board electronic components and train coupler equipment.

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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, as well as commuter rail locomotives.

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 in the fourth quarter 2006, the Company transferred certain operations between the Freight and Transit Group to reflect a shift in the markets and customers served by those operations and to reflect the information used by the chief decision maker in evaluating the operations of the Company. In addition, beginning in the fourth quarter 2006, the Company has allocated certain corporate costs to the Freight and Transit groups to reflect the beneficial use of these costs by the specific groups. Prior period results have been adjusted for comparability purposes.

Segment financial information for the three months ended June 30, 2007 is as follows:

| <i>In thousands</i> | Freight Group | Transit Group | Corporate Activities and Elimination | Total |
|--|----------------------|----------------------|---|-------------------|
| Sales to external customers | \$ 180,986 | \$ 144,736 | \$ | \$ 325,722 |
| Intersegment sales/(elimination) | 3,703 | 231 | (3,934) | |
| Total sales | \$ 184,689 | \$ 144,967 | \$ (3,934) | \$ 325,722 |
| Income (loss) from operations | \$ 30,906 | \$ 18,981 | \$ (4,118) | \$ 45,769 |
| Interest expense and other | | | (2,175) | (2,175) |
| Income (loss) from continuing operations before income taxes | \$ 30,906 | \$ 18,981 | \$ (6,293) | \$ 43,594 |

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

| <i>In thousands</i> | Freight Group | Transit Group | Corporate Activities and Elimination | Total |
|--|----------------------|----------------------|---|-------------------|
| Sales to external customers | \$ 180,169 | \$ 81,733 | \$ | \$ 261,902 |
| Intersegment sales/(elimination) | 3,285 | 145 | (3,430) | |
| Total sales | \$ 183,454 | \$ 81,878 | \$ (3,430) | \$ 261,902 |
| Income (loss) from operations | \$ 30,849 | \$ 7,776 | \$ (3,268) | \$ 35,357 |
| Interest expense and other | | | (1,854) | (1,854) |
| Income (loss) from continuing operations before income taxes | \$ 30,849 | \$ 7,776 | \$ (5,122) | \$ 33,503 |

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WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007 (UNAUDITED)

Segment financial information for the six months ended June 30, 2007 is as follows:

| <i>In thousands</i> | Freight Group | Transit Group | Corporate Activities and Elimination | Total |
|----------------------------------|--------------------------|--------------------------|---|-------------------|
| Sales to external customers | \$ 365,653 | \$ 274,333 | \$ | \$ 639,986 |
| Intersegment sales/(elimination) | 7,407 | 453 | (7,860) | |
| Total sales | \$ 373,060 | \$ 274,786 | \$ (7,860) | \$ 639,986 |
| Income (loss) from operations | \$ 66,244 | \$ 29,596 | \$ (7,954) | \$ 87,886 |
| Interest expense and other | | | | |