

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORP
Form 10-K/A
May 14, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K /A

(AMENDMENT NO. 1)

Annual report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2003

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

25-1615902
(IRS Employer

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(Incorporation or organization)

(Identification No.)

1001 Air Brake Avenue

Wilmerding, Pennsylvania 15148
(Address of principal executive offices, including zip code)

(412) 825-1000
(Registrant's telephone number)

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

| <u>Title of Class</u> | <u>Name of Exchange on which registered</u> |
|---|---|
| Common Stock, par value \$.01 per share | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the Act: None

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 at least the past 90 days. Yes No .

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No .

The registrant estimates that as of June 30, 2003, the aggregate market value of the voting shares held by non-affiliates of the registrant was approximately \$448 million based on the closing price on the New York Stock Exchange for such stock.

As of March 11, 2004, 44,687,830 shares of Common Stock of the registrant were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the Proxy Statement for the registrant's Annual Meeting of Stockholders to be held on May 19, 2004 are incorporated by reference into Part III of this Form 10-K.

EXPLANATION

Set forth in this Form 10-K/A Amendment No. 1 is an amendment relating to Item 15 (a) (1) of Part IV of the Annual Report of Westinghouse Airbrake Technologies Corporation on Form 10-K for the year ended December 31, 2003. The Report of Independent Auditors (Ernst & Young LLP) as reproduced in the Securities and Exchange Commission's EDGAR system omitted the City and State where issued, as required by Regulation S-X, Article 2-02(a)(3). This report has been corrected herein and issued along with the financial statements as of December 31, 2003 and 2002, and the results of operations and cash flows for the years then ended, which financial statements have not been amended in any manner. In connection with this amendment, the registrant is also amending the Exhibit Index in Item 15 (c) to include a new Consent of Ernst & Young LLP as Exhibit 23.1 and new certifications as Exhibits 31.2 and 32.2.

PART IV**Item 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K**

The financial statements, financial statement schedules and exhibits listed below are filed as part of this amended annual report:

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| (a) (1) Financial Statements | |
| <u>Report of Independent Auditors (Ernst & Young LLP)</u> | 6 |
| <u>Report of Independent Auditors (Arthur Andersen LLP)</u> | 7 |
| <u>Consolidated Balance Sheets as of December 31, 2003 and 2002</u> | 8 |
| <u>Consolidated Statements of Operations for the three years ended December 31, 2003, 2002 and 2001</u> | 9 |
| <u>Consolidated Statements of Cash Flows for the three years ended December 31, 2003, 2002 and 2001</u> | 10 |
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| (2) Financial Statement Schedules | |
| Schedule II - Valuation and Qualifying Accounts | |
| (b) Reports on Form 8-K | |

During the fourth quarter of 2003, the Company filed or furnished the following Current Reports on Form 8-K pertaining to the following items:

(1) A report dated October 15, 2003, which included under Items 5 and 7, the press release dated October 15, 2003 announcing the signing of a contract to supply brakes, couplers and current collectors for New York City subway cars, and under Items 7 and 12, the press release, dated October 15, 2003 announcing the financial results of the Company for the quarter ended September 30, 2003.

(2) A report dated October 20, 2003, which included under Items 5 and 7, certain reclassifications to the Company's Form 10-K for the year ended December 31, 2002.

(c) Exhibits

| | | <u>Filing Method</u> |
|--------|---|----------------------|
| 2.1 | Amended and Restated Agreement and Plan of Merger, as amended (originally included as Annex A to the Joint Proxy Statement/Prospectus) | 8 |
| 3.1 | Restated Certificate of Incorporation of the Company dated January 30, 1995, as amended March 30, 1995 | 2 |
| 3.3 | Amended and Restated By-Laws of the Company, effective November 19, 1999 | 8 |
| 4.1(a) | Indenture with the Bank of New York as Trustee dated as of August 6, 2003 | 15 |
| 4.1(b) | Resolutions Adopted July 23, 2003 by the Board of Directors establishing the terms of the offering of up to \$150,000,000 aggregate principal amount of 6.875% Notes due 2013 | 15 |
| 4.2 | Purchase Agreement, dated July 23, 2003, by and between the Company and the initial purchasers | 15 |
| 4.3 | Exchange and Registration Rights Agreement, dated August 6, 2003 | 15 |
| 10.1 | MotivePower Stock Option Agreement (originally included as Annex B to the Joint Proxy Statement/Prospectus) | 8 |
| 10.2 | Westinghouse Air Brake Stock Option Agreement (originally included as Annex C to the Joint Proxy Statement/Prospectus) | 8 |
| 10.3 | Voting Agreement dated as of September 26, 1999 among William E. Kassling, Robert J. Brooks, Harvard Private Capital Holdings, Inc. Vestar Equity Partners, L.P. and MotivePower Industries, Inc. (originally included as Annex D to the Joint Proxy Statement/Prospectus) | 8 |
| 10.9 | Amended and Restated Refinancing Credit Agreement dated as of November 19, 1999 among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York (Schedules and Exhibits omitted) | 9 |
| 10.10 | Amended and Restated Stockholders Agreement dated as of March 5, 1997 among the RAC Voting Trust (Voting Trust), Vestar Equity Partners, L.P. (Vestar Equity), Harvard Private Capital Holdings, Inc. (Harvard), American Industrial Partners Capital Fund II, L.P. (AIP) and the Company | 5 |
| 10.12 | Indemnification Agreement dated January 31, 1995 between the Company and the Voting Trust Trustees | 2 |
| 10.13 | Agreement of Sale and Purchase of the North American Operations of the Railway Products Group, an operating division of American Standard Inc., dated as of 1990 between Rail Acquisition Corp. and American Standard Inc. (only provisions on indemnification are reproduced) | 2 |
| 10.14 | Letter Agreement (undated) between the Company and American Standard Inc. on environmental costs and sharing | 2 |
| 10.15 | Purchase Agreement dated as of June 17, 1992 among the Company, Schuller International, Inc., Manville Corporation and European Overseas Corporation (only provisions on indemnification are reproduced) | 2 |
| 10.16 | Asset Purchase Agreement dated as of January 23, 1995 among the Company, Pulse Acquisition Corporation, Pulse Electronics, Inc., Pulse Embedded Computer Systems, Inc. and the Pulse Shareholders (Schedules and Exhibits omitted) | 2 |
| 10.17 | License Agreement dated as of December 31, 1993 between SAB WABCO Holdings B.V. and the Company | 2 |
| 10.18 | Letter Agreement dated as of January 19, 1995 between the Company and Vestar Capital Partners, Inc. | 2 |
| 10.19 | Westinghouse Air Brake Company 1995 Stock Incentive Plan, as amended | 7 |
| 10.20 | Westinghouse Air Brake Company 1995 Non-Employee Directors Fee and Stock Option Plan, as amended | 9 |
| 10.22 | Letter Agreement dated as of January 1, 1995 between the Company and Vestar Capital Partners, Inc. | 2 |

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| | | |
|-------|---|---|
| 10.23 | Form of Indemnification Agreement between the Company and Authorized Representatives | 2 |
| 10.27 | Amendment No. 1 to Amended and Restated Stockholders Agreement dated as of March 5, 1997 among the Voting Trust, Vestar, Harvard, AIP and the Company | 5 |
| 10.28 | Common Stock Registration Rights Agreement dated as of March 5, 1997 among the Company, Harvard, AIP and the Voting Trust | 5 |

| | | |
|-------|---|----|
| 10.29 | 1998 Employee Stock Purchase Plan | 7 |
| 10.32 | Westinghouse Air Brake Technologies Corporation 2000 Stock Incentive Plan | 10 |
| 10.33 | Amendment No. 1, dated as of November 16, 2000, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999 among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 11 |
| 10.34 | Amendment No. 2, dated as of March 30, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Chase Manhattan Bank as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.35 | Amendment No. 3, dated as of July 18, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Bank of New York, as co-syndication agent, The Chase Manhattan Bank as administrative agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.36 | Amendment No. 4, dated as of September 17, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, The Chase Manhattan Bank as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, LaSalle Bank National Association, The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.37 | Amendment No. 5, dated as of November 14, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, JP Morgan Chase Bank (formerly known as The Chase Manhattan Bank) as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.38 | Amendment No. 6, dated as of November 13, 2002, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, JP Morgan Chase Bank as administrative agent, and The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, LaSalle Bank National Association, as an issuing bank, ABN AMRO Bank N.V., as an issuing bank, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an | 14 |

| | | |
|-------|---|----|
| | issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 | |
| 10.39 | Asset Purchase Agreement, by and between General Electric Company, through its GE Transportation Systems business and Westinghouse Air Brake Technologies Corporation, dated as of July 24, 2001 | 12 |
| 10.40 | Refinancing Credit Agreement by and among the Company, the Guarantors, various lenders, LaSalle Bank National Association, JP Morgan Chase Bank, The Bank of New York, Citizens Bank of Pennsylvania, National City Bank of Pennsylvania, The Bank of Nova Scotia, Bank of Tokyo-Mitsubishi Trust Company and PNC Bank, National Association dated January 12, 2004 | 1 |
| 21 | List of subsidiaries of the Company | 1 |
| 23.1 | Consent of Ernst & Young LLP | 1 |
| 23.2 | Information Regarding Consent of Arthur Andersen LLP | 1 |
| 31.1 | Rule 13a-14(a)/15d-14(a) Certifications | 1 |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certifications | 1 |
| 32.1 | Section 1350 Certifications | 1 |
| 32.2 | Section 1350 Certifications | 1 |
| 99.1 | Annual Report on Form 11-K for the year ended December 31, 2003 of the Westinghouse Air Brake Technologies Corporation Savings Plan | 1 |
| 99.2 | Annual Report on Form 11-K for the year ended December 31, 2003 of the Westinghouse Air Brake Technologies Corporation Savings Plan for Hourly Employees | 1 |

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- 1 Filed herewith.
 - 2 Filed as an exhibit to the Company's Registration Statement on Form S-1 (No. 33-90866).
 - 3 Filed as an exhibit to the Company's Current Report on Form 8-K, dated October 3, 1996.
 - 4 Filed as an exhibit to the Company's Registration Statement on Form S-8 (No. 333-39159).
 - 5 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1997.
 - 6 Filed as an exhibit to the Company's Current Report on Form 8-K, dated October 5, 1998.
 - 7 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1998.
 - 8 Filed as part of the Company's Registration Statement on Form S-4 (No. 333-88903).
 - 9 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1999.
 - 10 Filed as an exhibit to the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2000.
 - 11 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2000.
 - 12 Filed as an exhibit to the Company's Current Report on Form 8-K, dated November 13, 2001.
 - 13 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2001.
 - 14 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2002.
 - 15 Filed as an exhibit to the Company's Registration Statement on Form S-4 (No. 333-110600).

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders of

Westinghouse Air Brake Technologies Corporation:

We have audited the accompanying consolidated balance sheet of Westinghouse Air Brake Technologies Corporation and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity and cash flows for the years then ended. Our audit also included the financial statement schedule for the year ended December 31, 2003 listed in the index in Item 15(a) of this Registration Statement. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Westinghouse Air Brake Technologies Corporation and subsidiaries as of December 31, 2001, and for the year then ended were audited by other auditors who have ceased operations. Those auditors expressed an unqualified opinion on those financial statements in their report dated February 18, 2002.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Westinghouse Air Brake Technologies Corporation and subsidiaries as of December 31, 2003 and 2002, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States. Also in our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As more fully discussed in Note 8 to the consolidated financial statements, effective January 1, 2002, Westinghouse Air Brake Technologies Corporation adopted the provisions of Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (SFAS No. 142).

As discussed above, the consolidated financial statements of Westinghouse Air Brake Technologies Corporation as of December 31, 2001, and for the year then ended were audited by other auditors who have ceased operations. As described in Note 8, these financial statements have been revised to include the transitional disclosures required by SFAS No. 142, which was adopted by the Company as of January 1, 2002. Our audit procedures with respect to the disclosures in Note 8 with respect to 2001 included (a) agreeing the previously reported net income to the previously issued financial statements and the adjustments to reported net income representing amortization expense (including any related tax effects) recognized in those periods related to goodwill as a result of initially applying Statement No. 142 to the Company's underlying records obtained from management, and (b) testing the mathematical accuracy of the reconciliation of adjusted net income to reported net income, and the related earnings per share amounts. In our opinion, the disclosures for 2001 in Note 8 are appropriate. However, we were not engaged to audit, review, or apply any procedures to the 2001 financial statements of the Company other than with respect to such disclosures and, accordingly, we do not express an opinion or any other form of assurance on the 2001 financial statements taken as a whole.

/s/ ERNST & YOUNG LLP

Pittsburgh, Pennsylvania

February 17, 2004

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders of

Westinghouse Air Brake Technologies Corporation:

We have audited the accompanying consolidated balance sheets of Westinghouse Air Brake Technologies Corporation (a Delaware corporation) and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Westinghouse Air Brake Technologies Corporation and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States.

/s/ ARTHUR ANDERSEN LLP

Pittsburgh, Pennsylvania

February 18, 2002

This is a copy of the audit report previously issued by Arthur Andersen LLP in connection with the Company's Annual Report on Form 10-K for the year ended December 31, 2001. This audit report has not been reissued by Arthur Andersen LLP in connection with this Annual Report Form 10-K. See Exhibit 23.2 for further discussion.

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

CONSOLIDATED BALANCE SHEETS

| <i>In thousands, except share and par value</i> | December 31, | |
|---|--------------|------------|
| | 2003 | 2002 |
| Assets | | |
| Current Assets | | |
| Cash | \$ 70,328 | \$ 19,210 |
| Accounts receivable | 129,074 | 108,019 |
| Inventories | 91,809 | 88,470 |
| Deferred income taxes | 23,457 | 23,613 |
| Other | 7,424 | 5,911 |
| Total current assets | 322,092 | 245,223 |
| Property, plant and equipment | 332,619 | 308,495 |
| Accumulated depreciation | (178,780) | (159,903) |
| Property, plant and equipment, net | 153,839 | 148,592 |
| Other Assets | | |
| Assets held for sale | 1,974 | 10,105 |
| Goodwill | 109,450 | 109,450 |
| Other intangibles, net | 37,776 | 41,524 |
| Deferred income taxes | 20,315 | 26,112 |
| Other noncurrent assets | 10,859 | 7,859 |
| Total other assets | 180,374 | 195,050 |
| Total Assets | \$ 656,305 | \$ 588,865 |
| Liabilities and Shareholders Equity | | |
| Current Liabilities | | |
| Current portion of long-term debt | \$ | \$ 833 |
| Accounts payable | 79,747 | 62,104 |
| Accrued income taxes | 126 | 3,928 |
| Customer deposits | 16,818 | 10,827 |
| Accrued compensation | 18,131 | 19,814 |
| Accrued warranty | 13,307 | 17,407 |
| Other accrued liabilities | 24,651 | 20,350 |
| Total current liabilities | 152,780 | 135,263 |
| Long-term debt | 190,225 | 194,318 |
| Reserve for postretirement and pension benefits | 39,055 | 38,266 |
| Deferred income taxes | 11,631 | 8,771 |
| Commitments and contingencies | 5,536 | 7,568 |
| Notes payable | 3,198 | |
| Other long-term liabilities | 5,587 | 5,417 |
| Total liabilities | 408,012 | 389,603 |
| Shareholders Equity | | |
| Preferred stock, 1,000,000 shares authorized, no shares issued | | |
| Common stock, \$.01 par value; 100,000,000 shares authorized: 66,174,767 and 65,447,867 shares issued and 44,631,733 and 43,440,840 outstanding at December 31, 2003 and 2002, respectively | 662 | 654 |

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| | | |
|--|-------------------|-------------------|
| Additional paid-in capital | 282,872 | 272,782 |
| Treasury stock, at cost, 21,543,034 and 22,007,027 shares, at December 31, 2003 and 2002, respectively | (267,586) | (273,634) |
| Retained earnings | 252,234 | 231,282 |
| Deferred compensation | | 270 |
| Accumulated other comprehensive loss | (19,889) | (32,092) |
| | <u>248,293</u> | <u>199,262</u> |
| Total shareholders' equity | | |
| | <u>\$ 656,305</u> | <u>\$ 588,865</u> |
| Total Liabilities and Shareholders' Equity | | |

The accompanying notes are an integral part of these statements.

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

| <i>In thousands, except per share data</i> | Year ended December 31, | | |
|--|-------------------------|-------------|------------|
| | 2003 | 2002 | 2001 |
| Net sales | \$ 717,924 | \$ 696,195 | \$ 783,698 |
| Cost of sales | (528,474) | (516,724) | (573,772) |
| Gross profit | 189,450 | 179,471 | 209,926 |
| Selling, general and administrative expenses | (100,503) | (93,023) | (96,723) |
| Merger and restructuring charges | | | (3,723) |
| Engineering expenses | (32,929) | (33,592) | (33,156) |
| Asset write-downs | | | (9,253) |
| Amortization expense | (4,309) | (5,322) | (13,013) |
| Total operating expenses | (137,741) | (131,937) | (155,868) |
| Income from operations | 51,709 | 47,534 | 54,058 |
| Other income and expenses | | | |
| Interest expense | (10,377) | (18,072) | (33,501) |
| Other expense, net | (6,290) | (5,558) | (2,130) |
| Income from continuing operations before income taxes and cumulative effect of accounting change | 35,042 | 23,904 | 18,427 |
| Income tax expense | (12,790) | (7,594) | (4,465) |
| Income from continuing operations before cumulative effect of accounting change | 22,252 | 16,310 | 13,962 |
| Discontinued operations | | | |
| Income from discontinued operations (net of tax) | 451 | 403 | 6,360 |
| (Loss) gain on sale of discontinued operations (net of tax) | | (529) | 41,458 |
| Total discontinued operations | 451 | (126) | 47,818 |
| Income before cumulative effect of accounting change | 22,703 | 16,184 | 61,780 |
| Cumulative effect of accounting change for goodwill, net of tax | | (61,663) | |
| Net income (loss) | \$ 22,703 | \$ (45,479) | \$ 61,780 |
| Earnings Per Common Share | | | |
| Basic | | | |
| Income from continuing operations before cumulative effect of accounting change | \$ 0.51 | \$ 0.37 | \$ 0.33 |
| Income from discontinued operations | 0.01 | | 1.11 |
| Cumulative effect of accounting change | | (1.42) | |
| Net income (loss) | \$ 0.52 | \$ (1.05) | \$ 1.44 |
| Diluted | | | |
| Income from continuing operations before cumulative effect of accounting change | \$ 0.51 | \$ 0.37 | \$ 0.32 |
| Income from discontinued operations | 0.01 | | 1.11 |
| Cumulative effect of accounting change | | (1.41) | |
| Net income (loss) | \$ 0.52 | \$ (1.04) | \$ 1.43 |

| | | | |
|-------------------------------------|--------|--------|--------|
| Weighted average shares outstanding | | | |
| Basic | 43,538 | 43,291 | 42,949 |
| Diluted | 43,974 | 43,617 | 43,198 |

The accompanying notes are an integral part of these statements.

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

| <i>In thousands</i> | Year Ended December 31, | | |
|---|-------------------------|-------------|-----------|
| | 2003 | 2002 | 2001 |
| Operating Activities | | | |
| Net income (loss) | \$ 22,703 | \$ (45,479) | \$ 61,780 |
| Adjustments to reconcile net income to cash provided by operations: | | | |
| Cumulative effect of accounting change for goodwill, net of tax | | 61,663 | |
| Depreciation and amortization | 25,284 | 25,513 | 33,061 |
| Results of discontinued operations, net of tax | (451) | 126 | (47,818) |
| Loss on sale of product line | | | 521 |
| Write-down of assets | | | 9,253 |
| Deferred income taxes | 8,824 | 702 | (6,278) |
| Other, primarily non-cash portion of merger and restructuring charges | | | 160 |
| Discontinued operations | 107 | 58 | (1,213) |
| Changes in operating assets and liabilities, net of acquisitions | | | |
| Accounts receivable | (12,410) | (548) | 49,772 |
| Inventories | (796) | 17,812 | 12,670 |
| Accounts payable | 14,138 | (12,814) | (4,330) |
| Accrued income taxes | 286 | (30,262) | 5,021 |
| Accrued liabilities and customer deposits | 2,836 | 1,964 | (20,856) |
| Commitments and contingencies | (2,032) | (3,033) | (2,251) |
| Other assets and liabilities | (2,585) | (44) | 29,605 |
| Net cash provided by operating activities | 55,904 | 15,658 | 119,097 |
| Investing Activities | | | |
| Purchase of property, plant and equipment | (17,470) | (14,137) | (20,674) |
| Proceeds from disposal of property, plant and equipment | 5,048 | 3,673 | 5,873 |
| Acquisitions of businesses, net of cash acquired | | (1,654) | (3,730) |
| Cash received from disposition of discontinued operations | | 1,400 | 240,900 |
| Cash received from disposition of product line | | | 4,120 |
| Discontinued operations | (127) | (99) | 924 |
| Net cash (used for) provided by investing activities | (12,549) | (10,817) | 227,413 |
| Financing Activities | | | |
| (Repayments) borrowings of credit agreements | (149,700) | 129,700 | (298,000) |
| Borrowings (repayments) of senior notes | 150,000 | (175,000) | |
| Repayments of other borrowings | (5,249) | (641) | (280) |
| Stock issuance | 9,977 | | |
| Purchase of treasury stock | | | (585) |
| Proceeds from treasury stock from stock based benefit plans | 5,899 | 3,695 | 3,359 |
| Cash dividends | (1,751) | (1,808) | (1,681) |
| Net cash provided by (used for) financing activities | 9,176 | (44,054) | (297,187) |
| Effect of changes in currency exchange rates | (1,413) | 4,474 | (1,445) |
| Increase (decrease) in cash | 51,118 | (34,739) | 47,878 |
| Cash, beginning of year | 19,210 | 53,949 | 6,071 |
| Cash, end of year | \$ 70,328 | \$ 19,210 | \$ 53,949 |

The accompanying notes are an integral part of these statements.

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

| <i>In thousands</i> | Comprehensive | Common Stock | Additional Paid-in Capital | Treasury Stock | Retained Earnings | Deferred Compensation | Accumulated Other Comprehensive Loss |
|--|--------------------|-----------------|----------------------------------|-------------------|----------------------|--------------------------|---|
| | Income (Loss) | | | | | | |
| Balance, December 31, 2000 | | \$ 654 | \$ 273,494 | \$ (281,665) | \$ 218,470 | \$ 900 | \$ (15,482) |
| Cash dividends | | | | | (1,681) | | |
| Purchase of treasury stock | | | | (585) | | | |
| Proceeds from treasury stock issued from the exercise of stock options and other benefit plans, net of tax | | | (820) | 4,398 | | 1 | |
| Compensatory stock options granted through a Rabbi Trust | | | | 363 | | (363) | |
| Net income | \$ 61,780 | | | | 61,780 | | |
| Translation adjustment | (5,170) | | | | | | (5,170) |
| Cumulative effect of change in accounting for derivative financial instruments, net of \$(665) tax | (1,234) | | | | | | (1,234) |
| Unrealized losses on derivatives designated and qualified as cash flow hedges, net of \$(705) tax | (1,310) | | | | | | (1,310) |
| Additional minimum pension liability, net of \$(4,144) tax | (6,479) | | | | | | (6,479) |
| | <u>\$ 47,587</u> | | | | | | |
| Balance, December 31, 2001 | | \$ 654 | \$ 272,674 | \$ (277,489) | \$ 278,569 | \$ 538 | \$ (29,675) |
| Cash dividends | | | | | (1,808) | | |
| Proceeds from treasury stock issued from the exercise of stock options and other benefit plans, net of tax | | | 108 | 3,587 | | | |
| Compensatory stock options granted through a Rabbi Trust | | | | 268 | | (268) | |
| Net loss | \$ (45,479) | | | | (45,479) | | |
| Translation adjustment | 3,165 | | | | | | 3,165 |
| Unrealized gains on derivatives designated and qualified as cash flow hedges, net of \$755 tax | 1,538 | | | | | | 1,538 |
| Additional minimum pension liability, net of \$(4,551) tax | (7,120) | | | | | | (7,120) |
| | <u>\$ (47,896)</u> | | | | | | |
| Balance, December 31, 2002 | | \$ 654 | \$ 272,782 | \$ (273,634) | \$ 231,282 | \$ 270 | \$ (32,092) |
| Cash dividends | | | | | (1,751) | | |
| Stock issuance | | 8 | 9,969 | | | | |
| Proceeds from treasury stock issued from the exercise of stock options and other benefit plans, net of tax | | | 121 | 5,778 | | | |

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| | | | | | | |
|--|----|---------|------------|--------------|------------|-------------|
| Compensatory stock options granted through a Rabbi Trust | | | 270 | | (270) | |
| Net income | \$ | 22,703 | | 22,703 | | |
| Translation adjustment | | 13,962 | | | | 13,962 |
| Unrealized gains on other derivatives, net of \$135 tax | | 235 | | | | 235 |
| Unrealized gains on derivatives designated and qualified as cash flow hedges, net of \$496 tax | | 799 | | | | 799 |
| Additional minimum pension liability, net of \$(728) tax | | (2,793) | | | | (2,793) |
| | \$ | 34,906 | | | | |
| Balance, December 31, 2003 | | \$ 662 | \$ 282,872 | \$ (267,586) | \$ 252,234 | \$ (19,889) |

The accompanying notes are an integral part of these statements

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 certain markets 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 nine countries. In 2003, about 79 percent of the Company's revenues came from its North American operations, but Wabtec also sold products or services in 62 countries around the world.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation The consolidated financial statements include the accounts of the Company and its majority owned subsidiaries. Such statements have been prepared in accordance with generally accepted accounting principles. Sales between subsidiaries are billed at prices consistent with sales to third parties and are eliminated in consolidation.

Cash Equivalents Cash equivalents are highly liquid investments purchased with an original maturity of three months or less.

Allowance for Doubtful Accounts The allowance for doubtful accounts receivable reflects our best estimate of probable losses inherent in our receivable portfolio determined on the basis of historical experience, specific allowances for known troubled accounts and other currently available evidence. The allowance for doubtful accounts was \$4.5 million and \$4.6 million as of December 31, 2003 and 2002, respectively.

Inventories Inventories are stated at the lower of cost or market. Cost is determined under the first-in, first-out (FIFO) method. Inventory costs include material, labor and overhead.

Property, Plant and Equipment Property, plant and equipment additions are stated at cost. Expenditures for renewals and improvements are capitalized. Expenditures for ordinary maintenance and repairs are expensed as incurred. The Company provides for book depreciation principally on the straight-line method. Accelerated depreciation methods are utilized for income tax purposes.

Leasing Arrangements The Company conducts a portion of its operations from leased facilities and finances certain equipment purchases through lease agreements. In those cases in which the lease term approximates the useful life of the leased asset or the lease meets certain other prerequisites, the leasing arrangement is classified as a capital lease. The remaining arrangements are treated as operating leases.

Intangible Assets The Company adopted SFAS No. 142 effective January 1, 2002, and, as a result, goodwill and other intangible assets with indefinite lives are no longer amortized. Other intangibles (with definite lives) are amortized on a straight-line basis over their estimated economic lives. Goodwill effective January 1, 2002 is reviewed annually for impairment while amortizable intangibles are reviewed for impairment when indicators of impairment are present.

Warranty Costs Warranty costs are accrued based on management's estimates of repair or upgrade costs per unit and historical experience. In recent years, the Company has introduced a number of new products. The Company does not have the same level of historical warranty experience for these new products as it does for its continuing products. Therefore, warranty reserves have been established for these new products based upon management's estimates. Actual future results may vary from such estimates. Warranty expense was \$10.5 million, \$17.6 million and \$14.1 million for 2003, 2002 and 2001, respectively. Warranty reserves were \$13.3 million and \$17.4 million at December 31, 2003 and 2002, respectively.

Deferred Compensation Agreements In May 1998, a consensus on Emerging Issues Task Force Issue No. 97-14, Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested (EITF 97-14), was issued. The adoption of EITF 97-14 required the Company to record as treasury stock the historical value of the Company's stock maintained in its deferred compensation plans.

Income Taxes Income taxes are accounted for under the liability method. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The provision for income taxes includes federal, state and foreign income taxes.

Stock-Based Compensation Effective January 1, 2003, the Company adopted SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure. SFAS No. 148 amends SFAS No. 123, Accounting for Stock-Based Compensation, to provide alternate methods of transition to SFAS No. 123's fair value method of accounting for stock-based compensation. The statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures about the method of accounting for

compensation cost associated with employee stock option plans, as well as the effect of the method used on reported results. The Company adopted the disclosure requirements of SFAS No. 148 and has not changed its method for measuring the compensation cost of stock options.

The Company continues to use the intrinsic value based method and does not recognize compensation expense for the issuance of options with an exercise price equal to or greater than the market price of the stock at the time of grant. As a result, the adoption of SFAS No. 148 had no impact on our results of operations or financial position.

Had compensation expense for these plans been determined based on the fair value at the grant dates for awards, the Company's net income and earnings per share would be as set forth in the following table. For purposes of pro forma disclosures, the estimated fair value is amortized to expense over the options' vesting period.

| <i>In thousands, except per share</i> | For the year ended December 31, | | |
|---------------------------------------|------------------------------------|-------------|-----------|
| | 2003 | 2002 | 2001 |
| Net income (loss) | | | |
| As reported | \$ 22,703 | \$ (45,479) | \$ 61,780 |
| Stock based compensation under FAS123 | 1,940 | 1,635 | 3,089 |
| Pro forma | 20,763 | (47,114) | 58,691 |
| Basic earnings (loss) per share | | | |
| As reported | \$ 0.52 | \$ (1.05) | \$ 1.44 |
| Pro forma | 0.48 | (1.09) | 1.37 |
| Diluted earnings (loss) per share | | | |
| As reported | \$ 0.52 | \$ (1.04) | \$ 1.43 |
| Pro forma | 0.47 | (1.07) | 1.36 |

For purposes of presenting pro forma results, 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:

| | For the year ended December 31, | | |
|-------------------------|------------------------------------|-------|-------|
| | 2003 | 2002 | 2001 |
| Dividend yield | .3 % | .3 % | .3 % |
| Risk-free interest rate | 5.2 % | 5.6 % | 5.9 % |
| Stock price volatility | 46.1 | 46.7 | 47.3 |
| Expected life (years) | 5.0 | 5.0 | 5.0 |

The Black-Scholes option valuation model was developed for use in estimating fair value of traded options, which are significantly different than employee stock options. Although this valuation model is an acceptable method for use in presenting pro forma information, because of the differences in traded options and employee stock options, the Black-Scholes model does not necessarily provide a single measure of the fair

value of employee stock options.

Financial Derivatives and Hedging Activities The Company periodically enters into interest rate swap agreements to reduce the impact of interest rate changes on its variable rate borrowings. Interest rate swaps are agreements with a counterparty to exchange periodic interest payments (such as pay fixed, receive variable) calculated on a notional principal amount. The interest rate differential to be paid or received is recognized as interest expense.

The Company has adopted Statement of Financial Accounting Standards (SFAS) No. 133, and as amended by SFAS 138, Accounting for Derivative Instruments and Hedging Activities effective January 1, 2001, resulting in the recording of current assets of \$266,000, long term assets of \$399,000, current liabilities of \$760,000, long term liabilities of \$1.1 million, and a decrease in other comprehensive loss of \$1.2 million. In the application, the Company has concluded its interest rate swap contracts qualify for special cash flow hedge accounting which permit recording the fair value of the swap and corresponding adjustment to other comprehensive income (loss) on the balance sheet. At December 31, 2003, and as a result of entering into these interest rate swaps, the Company is expected to incur \$600,000 in additional interest expense in 2004.

The Company also entered into foreign currency options and forward contracts to reduce the impact of changes in currency exchange rates. A currency option gives the Company the right but not the obligation to exchange currency at a pre-determined exchange rate either on a specific date or within a specific period of time. 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. All outstanding forward contracts and option agreements are for the sale of U.S. Dollars and the purchase of Canadian Dollars (CAD). As of December 31, 2003, the Company has outstanding option agreements with a notional value of \$10.5 million CAD resulting in the recording of a current asset of \$270,000, and an increase in comprehensive income of \$171,000, net of tax and has forward contracts with a notional value of \$13.5 million CAD, resulting in the recording of a current asset of \$100,000, and an increase in comprehensive income of \$64,000, net of tax. At December 31, 2003, and as a result of entering into these foreign currency forward and option contracts, the Company is not expected to incur any additional currency exchange loss or gain in 2004.

Subsequent to December 31, 2003, The Company entered into additional forward contracts to hedge its exposure to Canadian currency risk. Including the forwards outstanding at the end of 2003, the forward contracts currently have a total notional value of \$83 million CAD (or \$62 million U.S.), with an average exchange rate of \$0.747 USD per \$1 CAD.

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 Statement of Financial Accounting Standards (SFAS) No. 52, Foreign Currency Translation. The effects of currency exchange rate changes on intercompany transactions and balances of a long-term investment nature are accumulated and carried as a component of shareholders' equity. The effects of currency exchange rate changes on intercompany transactions that are non U.S. dollar denominated amounts are charged or credited to earnings. Foreign exchange loss was \$2.8 million, \$1.2 million and \$1.7 million for 2003, 2002 and 2001, respectively.

Other Comprehensive Income (Loss) Comprehensive income (loss) is defined as net income and all other non-owner changes in shareholders' equity. The Company's accumulated other comprehensive income (loss) consists of foreign currency translation adjustments, unrealized gains and losses on derivatives designated and qualified as cash flow hedges, foreign currency hedges and pension related adjustments.

Revenue Recognition Revenue is recognized in accordance with Staff Accounting Bulletin (SAB) 101, Revenue Recognition in Financial Statements. Wabtec recognizes revenue upon the passage of title, ownership and risk of loss to the customer.

The Company recognizes revenues on long-term contracts based on the percentage of completion method of accounting. Contract revenues and cost estimates are reviewed and revised quarterly, at a minimum, and adjustments are reflected in the accounting period as known. Provisions are made for estimated losses on uncompleted contracts as known, if necessary. Certain pre-production costs relating to long term production and supply contracts have been deferred and will be amortized over the life of the contract. Deferred pre-production costs were \$3.4 million and \$700,000 at December 31, 2003 and 2002, respectively.

Significant Customers and Concentrations of Credit Risk The Company's trade receivables are primarily from rail and transit industry original equipment manufacturers, Class I railroads, railroad carriers and commercial companies that utilize rail cars in their operations, such as utility and chemical companies. No one customer accounted for more than 10% of the Company's consolidated net sales in 2003. One customer, in the transit group, accounted for 11% of the Company's consolidated net sales in 2002 and 2001.

Shipping and Handling Fees and Costs All fees billed to the customer for shipping and handling are classified as a component of net revenues. All costs associated with shipping and handling is classified as a component of cost of sales.

Research and Development Research and development costs are charged to expense as incurred. For the years ended December 31, 2003, 2002 and 2001, the Company incurred costs of approximately \$32.9 million, \$33.6 million and \$33.2 million, respectively.

Employees As of December 31, 2003, approximately 36% of the Company's workforce was covered by collective bargaining agreements. These agreements are generally effective through 2004, 2005 and 2006.

Earnings Per Share Basic earnings per common share are computed by dividing net income applicable to common shareholders by the weighted-average number of shares of common stock outstanding during the year. Diluted earnings per common share are computed by dividing net income applicable to common shareholders by the weighted average number of shares of common stock outstanding adjusted for the assumed conversion of all dilutive securities (such as employee stock options).

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

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.

Recent Accounting Pronouncements. In April 2003, the Financial Accounting Standards Board issued SFAS No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities. SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. The provisions of this statement are effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003 and should be applied prospectively. SFAS No. 149 has no impact on the Company's financial statements or results of operations.

In May 2003, the Financial Accounting Standards Board issued SFAS No. 150, Accounting for Certain Instruments with Characteristics of Both Liabilities and Equity. SFAS No. 150 requires that certain financial instruments embodying an obligation to transfer assets or to issue equity securities be classified as liabilities. It is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective July 1, 2003. SFAS No. 150 has no impact on the Company's financial statements or results of operations.

Effective December 31, 2003, Wabtec adopted SFAS No. 132 (revised 2003), Employers' Disclosures about Pensions and Other Post-retirement Benefits an Amendment of FASB Statements No. 87, 88 and 106 for its U.S. pension plans. This standard requires additional disclosures about an employer's pension plans and postretirement benefits such as: the type of plan assets, investment strategy, measurement date, plan obligations, cash flows, and components of net periodic benefit costs recognized during interim periods. See Note 10 to the Consolidated Financial Statements for the required additional disclosures.

During 2003, the Company adopted FASB Interpretation No. (FIN) 45, Guarantors' Accounting and Disclosure Requirements for Guarantees. FIN 45 requires increased disclosure of guarantees, including those for which likelihood payment is remote, and product warranty information (see Note 16). FIN 45 also requires that guarantors recognize a liability for certain types of guarantees equal to the fair value of the guarantee upon its issuance. The adoption of FIN 45 has no impact on the Company's financial statements or results of operations.

In January 2003, the Financial Accounting Standards Board issued Interpretation No. 46, Consolidation of Variable Interest Entities. A variable interest entity (VIE) is one where the contractual or ownership interests in an entity change with changes in the entity's net asset value. This interpretation requires the consolidation of a VIE by the primary beneficiary, and also requires disclosure about VIEs where an enterprise has a significant variable interest but is not the primary beneficiary. The Company does not believe that this statement will have a material impact on the Company's financial statements or results of operations.

On December 8, 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act). The Act expanded Medicare to include, for the first time, coverage for prescription drugs. In January 2004, the FASB issued Staff Position 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003, (FSP FAS 106-1). This position permits a sponsor of a postretirement health care plan that provides a prescription drug benefit to make a one-time election to defer accounting for the effects of the Act. As permitted by FSP FAS 106-1, the Company has elected to defer financial recognition of this legislation until the FASB issues final accounting guidance. In accordance with FSP FAS 106-1, appropriate disclosures related to the deferral election have been made in Note 10 to the consolidated financial statements.

3. DISCONTINUED OPERATIONS

On November 1, 2001, the Company completed the sale of certain assets to GE Transportation Systems (GETS) for \$238 million in cash. The assets sold primarily included locomotive aftermarket products and services for which Wabtec was not the original equipment manufacturer. Under the terms of the sales agreement, the Company has agreed to indemnify GETS for, among other things, certain potential third party, off site environmental cleanup or remediation costs. The Company has purchased an insurance policy to mitigate its exposure for the environmental indemnities. The Company reported a \$48.7 million after tax gain on the sale in 2001.

In the fourth quarter of 2001, the Company decided to exit other businesses and put these businesses up for sale. The net assets of those businesses were written down to their estimated realizable value based on a multiple of earnings and was classified as Assets Held for Sale on the balance sheet. The Company reported a \$7.2 million after tax loss on the write-down of these entities.

As of December 31, 2003, one of the businesses has not sold. The Company actively solicited but did not receive any reasonable offers to purchase the asset and, in response, had reduced the price. The asset is no longer being actively marketed and as a result, the Company reclassified the business to continuing operations in the fourth quarter of 2003. Such reclassification had no material impact on the financial statements.

In accordance with SFAS 144, the operating results of these businesses have been classified as discontinued operations for all years presented and are summarized as of December 31, as follows:

| <i>In thousands</i> | For the year ended December 31, | | |
|-------------------------------------|---------------------------------|-----------|------------|
| | 2003 | 2002 | 2001 |
| Net sales | \$ 6,593 | \$ 11,158 | \$ 156,803 |
| Income before income taxes | 710 | 593 | 9,785 |
| Income tax expense | 259 | 190 | 3,425 |
| Income from discontinued operations | \$ 451 | \$ 403 | \$ 6,360 |

4. SUPPLEMENTAL CASH FLOW DISCLOSURES

| <i>In thousands</i> | For the year ended December 31, | | |
|-----------------------------------|---------------------------------|-----------|-----------|
| | 2003 | 2002 | 2001 |
| Interest paid during the year | \$ 6,478 | \$ 18,111 | \$ 37,181 |
| Income taxes paid during the year | 8,185 | 34,452 | 8,318 |
| Business acquisitions: | | | |
| Fair value of assets acquired | \$ | \$ 1,654 | \$ 5,275 |
| Liabilities assumed | | | (842) |
| Cash paid | | 1,654 | 4,433 |
| Less cash acquired | | | 703 |
| Net cash paid | \$ | \$ 1,654 | \$ 3,730 |

| | _____ | _____ | _____ |
|---|----------|--------|--------|
| Noncash investing and financing activities: | | | |
| Notes payable | \$ 3,198 | | |
| Deferred compensation | \$ 270 | \$ 268 | \$ 363 |
| Treasury stock | (270) | (268) | (363) |

5. MERGERS AND ACQUISITIONS

The Company did not make any acquisitions in 2003. During 2002 and 2001 the Company completed the following acquisitions:

- i) In February 2002, the Company purchased the minority interest of a business in India that the Company did not already own for \$1.7 million.
- ii) In October 2001, the Company purchased certain assets of Milufab, a supplier of door panels for subway trains for \$3.7 million.

These acquisitions were accounted for under the purchase method. Accordingly, the results of operations of the applicable acquisition are included in the Company's financial statements prospectively from the acquisition date. The excess of the purchase price over the fair value of identifiable net assets was approximately \$2.9 million and was allocated to goodwill. Effective January 1, 2002, goodwill was no longer amortized upon adoption of SFAS No. 142.

6. INVENTORY

The components of inventory, net of reserves, were:

| <i>In thousands</i> | December 31, | |
|------------------------|------------------|------------------|
| | 2003 | 2002 |
| Raw materials | \$ 28,711 | \$ 56,016 |
| Work-in-process | 45,559 | 27,856 |
| Finished goods | 17,539 | 4,598 |
| Total inventory | \$ 91,809 | \$ 88,470 |

7. PROPERTY, PLANT & EQUIPMENT

The major classes of depreciable assets are as follows:

| <i>In thousands</i> | December 31, | |
|----------------------------|--------------|------------|
| | 2003 | 2002 |
| Machinery and equipment | \$ 249,604 | \$ 229,813 |
| Buildings and improvements | 76,290 | 72,848 |
| Land and improvements | 6,435 | 5,572 |
| Locomotive leased fleet | 290 | 262 |

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| | | |
|--------------------------------|-------------------|-------------------|
| PP&E | 332,619 | 308,495 |
| Less: accumulated depreciation | (178,780) | (159,903) |
| | <u> </u> | <u> </u> |
| Total | \$ 153,839 | \$ 148,592 |
| | <u> </u> | <u> </u> |

The estimated useful lives of property, plant and equipment are as follows:

| | <u>Years</u> |
|----------------------------|--------------|
| Land improvements | 10 to 20 |
| Buildings and improvements | 20 to 40 |
| Machinery and equipment | 3 to 15 |
| Locomotive leased fleet | 4 to 15 |

Depreciation expense was \$21 million, \$20.2 million and \$20 million for 2003, 2002 and 2001, respectively.

8. INTANGIBLES

The Company has adopted SFAS No. 142, *Goodwill and Other Intangible Assets* effective January 1, 2002. Under its provisions, all goodwill and other intangible assets with indefinite lives are no longer amortized under a straight-line basis over the assets estimated useful life. Instead, they will be subject to periodic assessments for impairment by applying a fair-value-based test. In 2002, the Company completed the Phase I and Phase II assessments and wrote down the carrying value of goodwill by \$90 million (\$83.2 million for the Freight Group and \$6.8 million for the Transit Group), resulting in a non-cash after-tax charge of \$61.7 million. The fair value of these reporting units was determined using a combination of discounted cash flow analysis and market multiples based upon historical and projected financial information. The Company also performed the required impairment test in 2003 which resulted in no additional impairment charge. Goodwill still remaining on the balance sheet is \$109.5 million at December 31, 2003.

As of December 31, 2003 and 2002, the Company's trademarks had a net carrying amount of \$19.5 million 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> | December 31, | |
|--|------------------|------------------|
| | 2003 | 2002 |
| Patents and other, net of accumulated amortization of \$21,053 and \$18,492 | \$ 13,675 | \$ 16,124 |
| Covenants not to compete, net of accumulated amortization of \$9,437 and \$7,632 | 137 | 1,480 |
| Intangible pension asset | 4,401 | 4,357 |
| Total | \$ 18,213 | \$ 21,961 |

In connection with the adoption of SFAS No. 142, the Company reassessed the useful lives and the classification of its identifiable assets and determined that they continue to be appropriate. The weighted average useful life of patents was 13 years and of covenants not to compete was five years.

Amortization expense for intangible assets was \$3.4 million, \$4 million and \$11.3 million for the years ended December 31, 2003, 2002, and 2001, respectively. Amortization expense for the five succeeding years is as follows (in thousands):

| | |
|------|----------|
| 2004 | \$ 2,162 |
| 2005 | \$ 2,137 |
| 2006 | \$ 1,973 |
| 2007 | \$ 1,863 |
| 2008 | \$ 1,790 |

The changes in the carrying amount of goodwill by segment for the years ended December 31, 2003 and 2002, respectively, are as follows:

| <i>In thousands</i> | Freight Group | Transit Group | Total |
|---------------------|------------------|------------------|-------|
|---------------------|------------------|------------------|-------|

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| | | | |
|------------------------------|-------------------|-------------------|-------------------|
| Balance at December 31, 2001 | \$ 175,085 | \$ 23,703 | \$ 198,788 |
| Goodwill acquired | 664 | | 664 |
| Goodwill written off | (83,179) | (6,823) | (90,002) |
| | <u> </u> | <u> </u> | <u> </u> |
| Balance at December 31, 2002 | \$ 92,570 | \$ 16,880 | \$ 109,450 |
| Goodwill acquired | | | |
| Goodwill written off | | | |
| | <u> </u> | <u> </u> | <u> </u> |
| Balance at December 31, 2003 | \$ 92,570 | \$ 16,880 | \$ 109,450 |
| | <u> </u> | <u> </u> | <u> </u> |

Actual results of continuing operations for the year ended December 31, 2003 and 2002, and pro forma results of continuing operations for 2001 had we applied the non-amortization provisions of SFAS No. 142 in these periods are as follows:

| <i>In thousands, except per share amounts</i> | For the year ended | | |
|---|--------------------|-----------|-----------|
| | December 31, | | |
| | 2003 | 2002 | 2001 |
| Reported income before cumulative effect of accounting change | \$ 22,703 | \$ 16,184 | \$ 61,780 |
| Add: goodwill amortization, net of tax | | | 4,147 |
| Add: trademark amortization, net of tax | | | 376 |
| Adjusted income before cumulative effect of accounting change | \$ 22,703 | \$ 16,184 | \$ 66,303 |
| Basic earnings per share | | | |
| Reported income before cumulative effect of accounting change | \$ 0.52 | \$ 0.37 | \$ 1.44 |
| Goodwill amortization | | | 0.09 |
| Trademark amortization | | | 0.01 |
| Adjusted income before cumulative effect of accounting change | \$ 0.52 | \$ 0.37 | \$ 1.54 |
| Diluted earnings per share | | | |
| Reported income before cumulative effect of accounting change | \$ 0.52 | \$ 0.37 | \$ 1.43 |
| Goodwill amortization | | | 0.09 |
| Trademark amortization | | | 0.01 |
| Adjusted income before cumulative effect of accounting change | \$ 0.52 | \$ 0.37 | \$ 1.53 |

9. LONG-TERM DEBT

Long-term debt consisted of the following:

| <i>In thousands</i> | December 31, | |
|---------------------------------------|--------------|------------|
| | 2003 | 2002 |
| Revolving credit agreement due 2004 | \$ 40,000 | \$ 189,700 |
| 6.875% Senior notes | 150,000 | |
| 5.5% Industrial revenue bond due 2008 | | 4,909 |
| Other | 225 | 542 |
| Total | \$ 190,225 | \$ 195,151 |
| Less current portion | | 833 |
| Long term portion | \$ 190,225 | \$ 194,318 |

Credit Agreement

In November 1999, Wabtec refinanced the then existing unsecured MotivePower credit agreement (the Credit Agreement) with a consortium of commercial banks. This unsecured Credit Agreement provided a \$275 million five-year revolving credit facility expiring in November 2004 and a 364-day \$275 million convertible revolving credit facility maturing in November 2004. In November 2001, the Company and the banks negotiated a reduction in the 364-day facility to \$100 million, as a result of the \$208 million, net of tax, cash proceeds from the sale of certain businesses. In November 2002, the Company negotiated a further reduction in the 364-day facility from \$100 million to \$95 million. In July 2003, the Company and the banks negotiated a reduction in both facilities to \$225 million as a result of the issuance of the Senior Notes. The \$225 million facility provided a reduced five-year facility of \$167.2 million and a reduced 364-day facility of \$57.8 million. In November 2003, the Company allowed the \$57.8 million 364-day facility to expire. At December 31, 2003, the Company's available bank borrowing capacity, net of \$19.6 million of letters of credit, was approximately \$107.7 million.

Credit Agreement borrowings bear variable interest rates indexed to the indices described below. The maximum credit agreement borrowings, average credit agreement borrowings and weighted-average contractual interest rate on credit agreement borrowings were \$209 million, \$129.3 million and 2.68%, respectively for 2003. To reduce the impact of interest rate changes on a portion of this variable-rate debt, the Company entered into interest rate swaps which effectively convert a portion of the debt from variable to fixed-rate borrowings during the term of the swap contracts. On December 31, 2003, the notional value of interest rate swaps outstanding totaled \$40 million and effectively changed the Company's interest rate on bank debt at December 31, 2003 from a variable rate to a fixed rate of 3.98%. The interest rate swap agreements mature in February 2006. The Company is exposed to credit risk in the event of

nonperformance by the counterparties. However, since only the cash interest payments are exchanged, exposure is significantly less than the notional amount. The counterparties are large financial institutions and the Company does not anticipate nonperformance.

As required by SFAS 145, the Company has reclassified a \$1.2 million net of tax charge related to the early extinguishment of debt in the third quarter of 2002, which had been previously recorded as an extraordinary item, to interest expense and income tax expense.

Refinancing Credit Agreement

In January 2004, the Company entered into a new credit agreement, refinancing its existing unsecured revolving Credit Agreement with a consortium of commercial banks. This Refinancing Credit Agreement provides a \$175 million five-year revolving credit facility expiring in January 2009. The financial statements have been prepared based on the terms of the Refinanced Credit Agreement.

Under the Refinancing Credit Agreement, the Company may elect a base rate or an interest rate based on the London Interbank Offered Rates of Interest (LIBOR). The base rate is the greater of LaSalle Bank National Association's prime rate or the federal funds effective rate plus 0.5% per annum. The LIBOR rate is based on LIBOR plus a margin that ranges from 100 to 200 basis points depending on the Company's consolidated total indebtedness to cash flow ratios. The current margin is 175 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.

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 will accrue at a rate of 6.875% per annum and will be payable semi-annually on January 31 and July 31 of each year, commencing on January 31, 2004. The proceeds were used to repay debt outstanding under the Company's existing credit agreement, and for general corporate purposes.

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

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Scheduled principal repayments of outstanding loan balances required as of December 31, 2003 are as follows:

| <i>In thousands</i> | <u>Original</u> | <u>As refinanced</u> |
|---------------------|-------------------|--------------------------|
| 2004 | \$ 40,000 | \$ |
| 2005 | 225 | 225 |
| 2006 | | |
| 2007 | | |
| 2008 | | |
| Future years | 150,000 | 190,000 |
| Total | <u>\$ 190,225</u> | <u>\$ 190,225</u> |

Extinguishment of Other Borrowings

In June 1995, the Company issued \$100 million of 9.375% Senior Notes due in 2005 (the 1995 Notes). In January 1999, the Company issued an additional \$75 million of 9.375% Senior Notes due in 2005 (the 1999 Notes). The 1995 Notes and the 1999 Notes were redeemed at par (face) on July 8, 2002 through the use of cash on hand and additional borrowings under the credit agreement. This redemption resulted in a non-cash loss of \$1.9 million relating to a write-off of deferred financing costs.

In July 1998, a subsidiary of the Company entered into a 10- year \$7.5 million debt obligation for the purchase of a building used in the Company's operations. The debt was repaid in September 2003.

10. EMPLOYEE BENEFIT PLANS

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

| <i>In thousands, except percentages</i> | For the years ended December 31, | | | |
|---|----------------------------------|-------------|----------------------|-------------|
| | Pension Plans | | Postretirement Plans | |
| | 2003 | 2002 | 2003 | 2002 |
| Defined Benefit Plans | | | | |
| Change in benefit obligation | | | | |
| Obligation at beginning of year | \$ (92,751) | \$ (89,449) | \$ (23,700) | \$ (21,368) |
| Service cost | (2,425) | (2,658) | (330) | (232) |
| Interest cost | (6,474) | (6,008) | (1,715) | (1,447) |
| Special termination benefits | | (1,241) | | |
| Actuarial (loss) gain | (7,762) | 2,767 | (5,495) | (2,581) |
| Benefits paid | 5,666 | 5,634 | 2,150 | 1,928 |
| Expenses paid | 372 | 326 | | |
| Effect of currency rate changes | (9,743) | (2,122) | | |
| Obligation at end of year | \$ (113,117) | \$ (92,751) | \$ (29,090) | \$ (23,700) |
| Change in plan assets | | | | |
| Fair value of plan assets at beginning of year | \$ 67,600 | \$ 77,711 | | |
| Actual gain (loss) on plan assets | 11,834 | (8,732) | | |
| Employer contribution | 5,554 | 2,465 | | |
| Participant contributions | 401 | 353 | | |
| Benefits paid | (5,666) | (5,634) | | |
| Administrative expenses | (1,081) | (695) | | |
| Effect of currency rate changes | 7,939 | 2,132 | | |
| Fair value of plan assets at end of year | \$ 86,581 | \$ 67,600 | | |
| Funded status | | | | |
| Funded status at year end | \$ (26,536) | \$ (25,151) | (29,090) | (23,700) |
| Unrecognized net actuarial loss | 29,213 | 25,628 | 8,961 | 3,922 |
| Unrecognized prior service cost | 4,237 | 4,376 | 22 | 34 |
| Unrecognized transition obligation | 3,084 | 3,031 | 194 | 216 |
| Effect of currency exchange rates | 1,399 | 139 | | |
| Prepaid (accrued) benefit cost | \$ 11,397 | \$ 8,023 | \$ (19,913) | \$ (19,528) |
| Amounts recognized in the statement of financial position include: | | | | |
| Prepaid pension cost | \$ 323 | \$ 110 | \$ | \$ |
| Reserve for postretirement and pension benefits | (19,142) | (18,738) | (19,913) | (19,528) |
| Intangible asset | 4,401 | 4,357 | | |

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| | | | | |
|--------------------------------------|-------------------|-------------------|-------------------|-------------------|
| Accumulated other comprehensive loss | 25,815 | 22,294 | | |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Prepaid (accrued) benefit cost | \$ 11,397 | \$ 8,023 | \$ (19,913) | \$ (19,528) |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |

| | Pension Plans | | | Postretirement Plans | | |
|-----------------------------------|-----------------|-----------------|---------------|----------------------|-----------------|-----------------|
| | 2003 | 2002 | 2001 | 2003 | 2002 | 2001 |
| Net periodic benefit cost | | | | | | |
| Service cost | \$ 2,425 | \$ 2,658 | \$ 1,447 | \$ 330 | \$ 232 | \$ 240 |
| Interest cost | 6,474 | 6,008 | 4,382 | 1,715 | 1,447 | 1,524 |
| Expected return on plan assets | (6,576) | (6,591) | (5,846) | | | |
| Net amortization/deferrals | 1,406 | 617 | 680 | 489 | 19 | (3) |
| Net periodic benefit cost | \$ 3,729 | \$ 2,692 | \$ 663 | \$ 2,534 | \$ 1,698 | \$ 1,761 |
| Assumptions | | | | | | |
| Discount rate | 6.25% | 6.75% | 7% | 6.25% | 6.75% | 7.5% |
| Expected long-term rate of return | 7.75% | 8.25% | 9% | NA | NA | NA |
| Rate of compensation increase | 3.75% | 4% | 5% | NA | NA | NA |

Included in the above table, the aggregate benefit obligation and fair value of plan assets for the pension plans with plan assets in excess of benefit obligations were \$3 million and \$3.4 million, respectively, as of December 31, 2003; and \$2 million and \$2.1 million, respectively, as of December 31, 2002 (the total of which was pension plan benefit obligation in excess of plan assets).

The components of prepaid (accrued) benefit costs by country are as follows:

| <i>In thousands</i> | 2003 | 2002 |
|---------------------------------------|------------------|-----------------|
| U.S. plan | \$ 1,539 | \$ 1,716 |
| Canadian plans | 10,103 | 6,307 |
| U.K. plan | (245) | |
| Prepaid (accrued) benefit cost | \$ 11,397 | \$ 8,023 |

Pension Plan Assets

The composition of U.S. plan assets consists primarily of equities, corporate bonds, governmental notes and temporary investments. This Plan's asset allocations at December 31, 2003 by asset category are as follows:

| Asset Category | % |
|-----------------------------------|-------------|
| Equity securities | 49% |
| Debt securities | 46% |
| Other, including cash equivalents | 5% |
| Total | 100% |

Investment policies are determined by the Plan's Pension Committee and set forth in the Plan's Investment Policy. Pursuant to the Plan's Investment Policy, the investment strategy is to use passive index funds managed by the Bank of New York. The target asset allocation and composite benchmarks include the following:

| Asset Allocation | | Composite Benchmark | |
|----------------------|------|---------------------|------|
| Category | % | Benchmark | % |
| Bonds | 50% | Lehman Aggregate | 50% |
| Large Cap Stocks | 35% | S&P 500 | 35% |
| International Stocks | 10% | MSCI-EAFE | 10% |
| Small Cap Stocks | 5% | Russell 2000 | 5% |
| | 100% | | 100% |

The Company's funding methods, which are primarily based on the ERISA requirements, differ from those 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 \$6.4 million to the pension plan during 2004 and that this level of funding to continue in future periods. Rebalancing of the asset allocation occurs on a quarterly basis.

In 2002, as a result of an early retirement package offered to certain union employees, the Company incurred charges of approximately \$1.2 million reflected above as a special termination benefit.

In addition to providing pension benefits, the Company has provided certain unfunded postretirement health care and life insurance benefits for substantially all U.S. employees. In January 1995 the postretirement health care and life insurance benefits for salaried employees was modified to discontinue benefits for employees who had not attained the age of 50 by March 31, 1995. The Company is not obligated to pay health care and life insurance benefits to individuals who had retired prior to 1990.

The assumed health care cost trend rate grades from an initial rate of 8% to an ultimate rate of 4.75% in four years. A 1% increase in the assumed health care cost trend rate will increase the amount of expense recognized for the postretirement plans by approximately \$358,000 for 2004, and increase the service and interest cost components of the accumulated postretirement benefit obligation by approximately \$4.1 million. A 1% decrease in the assumed health care cost trend rate will decrease the service and interest cost components of the expense recognized for the postretirement plans by approximately \$286,000 for 2004, and decrease the accumulated postretirement benefit obligation by approximately \$3.4 million.

On December 8, 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act). The Act expanded Medicare to include, for the first time, coverage for prescription drugs. The Company sponsors retiree medical programs for certain of its locations and expects that this legislation will reduce the Company's costs for some of these programs in the future.

In January 2004, FASB Staff Position 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (FSP FAS 106-1) was issued which permits a sponsor of a postretirement health care plan that provides a prescription drug benefit to make a one-time election to defer accounting for the effects of the Act. The Company is awaiting guidance from various governmental and regulatory agencies concerning the requirements that must be met to obtain these cost reductions as well as the manner in which such savings should be measured. Based on this preliminary analysis, it appears that some of the Company's retiree medical plans may need to be revised in order to qualify for beneficial treatment under the Act, while other plans can continue unchanged.

Defined Contribution Plans

The Company also participates in a variety of defined contribution, 401(k) and multiemployer pension, health and welfare plans. Additionally, the Company has stock option-based benefit and other plans further described in Note 14. Costs recognized under multi-employer and other defined contribution plans are summarized as follows:

| | For the year ended | | |
|---------------------|--------------------|-------------|-------------|
| | December 31, | | |
| <u>In thousands</u> | <u>2003</u> | <u>2002</u> | <u>2001</u> |
| | | | |

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| | | | |
|---|-------------------|-------------------|-------------------|
| Multi-employer pension and health & welfare plans | \$ 1,531 | \$ 1,310 | \$ 994 |
| 401(k) savings and other defined contribution plans | 6,828 | 6,929 | 8,172 |
| | <u> </u> | <u> </u> | <u> </u> |
| Total | \$ 8,359 | \$ 8,239 | \$ 9,166 |
| | <u> </u> | <u> </u> | <u> </u> |

The 401(k) savings plan is a participant directed defined contribution plan that holds shares of the Company's stock. At December 31, 2003 and 2002, the plan held on behalf of its participants about 776,000 shares with a market value of \$13.2 million, and 861,000 shares with a market value of \$12 million, respectively.

11. INCOME TAXES

In general, the Company is responsible for filing consolidated U.S., foreign and combined, unitary or separate state income tax returns. The Company is responsible for paying the taxes relating to such returns, including any subsequent adjustments resulting from the redetermination of such tax liabilities by the applicable taxing authorities.

The components of the income (loss) from continuing operations before provision for income taxes for the Company's domestic and foreign operations for the years ended December 31 are provided below:

| <i>In thousands</i> | For the year ended | | |
|-----------------------------------|--------------------|-----------|-----------|
| | December 31, | | |
| | 2003 | 2002 | 2001 |
| Domestic | \$ 35,470 | \$ 12,226 | \$ 10,287 |
| Foreign | (428) | 11,678 | 8,140 |
| Income from continuing operations | \$ 35,042 | \$ 23,904 | \$ 18,427 |

No provision has been made for U.S., state or additional foreign taxes related to undistributed earnings of foreign subsidiaries which have been or are intended to be permanently re-invested. It is not practical to estimate the income tax expense or benefit that might be incurred if these earnings were to be remitted to the U.S.

The consolidated provision (credit) for income taxes included in the Statement of Income consisted of the following:

| <i>In thousands</i> | For the year ended | | |
|-----------------------|--------------------|----------|-----------|
| | December 31, | | |
| | 2003 | 2002 | 2001 |
| Current taxes | | | |
| Federal | \$ 763 | \$ 609 | \$ 28,703 |
| State | 1,470 | (2,421) | 4,919 |
| Foreign | 1,993 | 2,876 | 3,345 |
| | \$ 4,226 | \$ 1,064 | \$ 36,967 |
| Deferred taxes | | | |
| Federal | 11,525 | (14,788) | 1,106 |
| State | 821 | (4,364) | 287 |
| Foreign | (3,522) | (2,716) | (325) |
| | 8,824 | (21,868) | 1,068 |

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| | | | |
|--------------------------|-----------|-------------|-----------|
| Total provision (credit) | \$ 13,050 | \$ (20,804) | \$ 38,035 |
|--------------------------|-----------|-------------|-----------|

Consolidated income tax provision (credit) is included in the Statement of Income as follows:

| <i>In thousands</i> | For the year ended | | |
|---|--------------------|-------------|-----------|
| | December 31, | | |
| | 2003 | 2002 | 2001 |
| Continuing operations | \$ 12,790 | \$ 7,594 | \$ 4,465 |
| Income (loss) from discontinued operations | 260 | (59) | 33,570 |
| Cumulative effect of accounting change for goodwill | | (28,339) | |
| Total provision (credit) | \$ 13,050 | \$ (20,804) | \$ 38,035 |

A reconciliation of the United States federal statutory income tax rate to the effective income tax rate on continuing operations for the years ended December 31 is provided below:

| <i>In thousands</i> | For the year ended December 31, | | |
|--------------------------------------|------------------------------------|-------|--------|
| | 2003 | 2002 | 2001 |
| U. S. federal statutory rate | 35.0% | 35.0% | 35.0% |
| State taxes | 2.4 | 3.6 | 3.6 |
| Resolution of prior year tax matters | (7.6) | | |
| Change in valuation allowance | 7.4 | | |
| State deferred rate adjustment | 2.7 | | |
| Foreign | 1.5 | 0.3 | 0.4 |
| Foreign tax credits | (2.5) | (2.1) | |
| Research and development credit | (2.4) | (3.3) | (15.9) |
| Other, net | | (1.5) | 1.1 |
| Effective rate | 36.5% | 32.0% | 24.2% |

Deferred income taxes result from temporary differences in the recognition of income and expense for financial and income tax reporting purposes. These deferred income taxes will be recognized as future tax benefits or costs when the temporary differences reverse.

Components of deferred tax assets and (liabilities) were as follows:

| <i>In thousands</i> | December 31, | |
|----------------------------------|--------------|-----------|
| | 2003 | 2002 |
| Deferred income tax assets: | | |
| Accrued expenses and reserves | \$ 4,342 | \$ 3,970 |
| Deferred comp/employee benefits | 4,439 | 5,484 |
| Pension | 15,491 | 15,354 |
| Inventory | 4,388 | 3,878 |
| Warranty reserve | 3,224 | 6,062 |
| Restructuring reserve | 1,026 | 1,479 |
| Environmental reserve | 408 | 715 |
| Federal net operating loss | | 303 |
| State net operating loss | 7,193 | 5,925 |
| Plant, equipment and intangibles | 1,366 | 10,139 |
| Federal credits | 5,615 | 3,982 |
| Foreign net operating loss | 7,164 | 2,146 |
| Foreign deferred net items | (4,028) | (3,917) |
| Gross deferred income tax assets | 50,628 | 55,520 |
| Valuation allowance | (18,487) | (14,566) |
| Total deferred income tax assets | \$ 32,141 | \$ 40,954 |

A valuation allowance is provided when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company has recorded a valuation allowance of \$18.5 million for certain net operating loss carryforwards and deferred tax assets anticipated to produce no tax benefit. The valuation allowance has increased in the current year by \$3.9 million to be applied against certain state and foreign deferred tax assets.

State and foreign net operating loss carryforwards exist in the amount of \$139 million and \$20.5 million, respectively, and are set to expire in various periods from 2006 to 2023. A valuation allowance has been established for certain of these net operating loss carryforwards.

Federal tax credits exist of approximately \$5.6 million which are comprised of Research and Experimentation credits available through 2023 and Alternative Minimum Tax credits available indefinitely.

12. EARNINGS PER SHARE

The computation of earnings per share from continuing operations is as follows:

| <i>In thousands, except per share</i> | For the year ended | | |
|---|--------------------|----------------|----------------|
| | December 31, | | |
| | 2003 | 2002 | 2001 |
| Basic | | | |
| Income from continuing operations before cumulative effect of accounting change applicable to common shareholders | \$ 22,252 | \$ 16,310 | \$ 13,962 |
| Divided by: | | | |
| Weighted average shares outstanding | 43,538 | 43,291 | 42,949 |
| Basic earnings from continuing operations before cumulative effect of accounting change per share | <u>\$ 0.51</u> | <u>\$ 0.37</u> | <u>\$ 0.33</u> |
| Diluted | | | |
| Income from continuing operations before cumulative effect of accounting change applicable to common shareholders | \$ 22,252 | \$ 16,310 | \$ 13,962 |
| Divided by the sum of: | | | |
| Weighted average shares outstanding | 43,538 | 43,291 | 42,949 |
| Assumed conversion of dilutive stock options | 436 | 326 | 249 |
| Diluted shares outstanding | <u>43,974</u> | <u>43,617</u> | <u>43,198</u> |
| Diluted earnings from continuing operations before cumulative effect of accounting change per share | <u>\$ 0.51</u> | <u>\$ 0.37</u> | <u>\$ 0.32</u> |

Options to purchase approximately 646,000, 2.1 million and 2.8 million shares of Common Stock were outstanding in 2003, 2002 and 2001, respectively, but were not included in the computation of diluted earnings per share because the options' exercise price exceeded the average market price of the common shares.

13. STOCK-BASED COMPENSATION PLANS

Stock Options Under the 2000 Stock Incentive Plan (the 2000 Plan), the Company may grant options to employees for an initial amount of 1.1 million shares of Common Stock. This amount is subject to annual modification based on a formula. Under the formula, 1.5% of total common shares outstanding at the end of the preceding fiscal year are added to shares available for grant under the 2000 Plan. Based on the adjustment, the Company had approximately 1.4 million shares available for 2003 grants and has available approximately 1.4 million shares through the end of fiscal 2004. The shares available for grants on any given date may not exceed 15% of Wabtec's total common shares outstanding. Generally, the options become exercisable over a three-year vesting period and expire ten years from the date of grant.

As part of a long-term incentive program, in 1998, the Company granted options to purchase up to 500,020 shares, to certain executives under a plan that preceded the 2000 Plan. The option price is \$20 per share. The options vest 100% after eight years and are subject to accelerated vesting after three years if the Company achieves certain earnings targets as established by the compensation committee of the board of directors. No further grants may be made under this plan.

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The Company also has a non-employee directors stock option plan under which 500,000 shares of Common Stock are reserved for issuance. Through year-end 2003, the Company granted nonqualified stock options to non-employee directors to purchase a total of 93,000 shares.

Employee Stock Purchase Plan In 1998, the Company adopted an employee discounted stock purchase plan (DSPP). The DSPP had 500,000 shares available for issuance. Participants can purchase the Company's common stock at 85% of the lesser of fair market value on the first or last day of each offering period. Stock outstanding under this plan at December 31, 2003 was 202,632 shares.

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A summary of the Company's stock option activity and related information for the years indicated follows:

| | 2003 | | 2002 | | 2001 | |
|--|-----------|---------------------------------|-----------|---------------------------------|-------------|---------------------------------|
| | Options | Weighted Average Exercise Price | Options | Weighted Average Exercise Price | Options | Weighted Average Exercise Price |
| Beginning of year | 4,977,296 | \$ 13.44 | 4,599,935 | \$ 13.76 | 5,389,397 | \$ 14.74 |
| Granted | 718,500 | 10.85 | 835,500 | 12.15 | 512,212 | 13.22 |
| Exercised | (360,883) | 11.77 | (192,779) | 11.60 | (210,660) | 10.40 |
| Canceled | (250,737) | 16.06 | (265,360) | 15.41 | (1,091,014) | 19.00 |
| End of year | 5,084,176 | \$ 13.08 | 4,977,296 | \$ 13.44 | 4,599,935 | \$ 13.76 |
| Exercisable at end of year | 3,834,069 | | 3,771,366 | | 3,738,562 | |
| Available for future grant | 1,394,818 | | 1,343,893 | | 1,432,980 | |
| Weighted average fair value of options granted during the year | \$ 4.34 | | \$ 5.20 | | \$ 5.98 | |

The following table summarizes information about stock options outstanding at December 31, 2003:

| Range of Exercise Prices | Number Outstanding As of 12/31/03 | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price | Number Exercisable As of 12/31/03 |
|--------------------------|-----------------------------------|---|---------------------------------|-----------------------------------|
| \$ 5.06 - \$ 5.43 | 44,416 | 5.9 | 5.31 | 44,416 |
| 9.54 - 9.54 | 530,999 | 6.9 | 9.54 | 530,999 |
| 9.88 - 10.86 | 1,111,050 | 7.9 | 10.72 | 431,550 |
| 11.00 - 12.98 | 1,260,824 | 7.0 | 12.20 | 716,547 |
| 13.18 - 13.98 | 356,274 | 7.5 | 13.25 | 329,944 |
| 14.00 - 14.00 | 1,134,881 | 1.8 | 14.00 | 1,134,881 |
| 14.63 - 19.91 | 109,900 | 4.8 | 17.71 | 109,900 |
| 20.00 - 20.00 | 404,200 | 4.8 | 20.00 | 404,200 |
| \$22.38 - \$29.61 | 131,632 | 4.5 | 24.88 | 131,632 |
| | 5,084,176 | 5.8 | \$ 13.08 | 3,834,069 |

Restricted Stock Award

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In February of 2001, the Company awarded to two officers 4,920 shares of restricted Common Stock in lieu of a cash bonus for 2000.

14. OTHER COMPREHENSIVE LOSS

The components of accumulated other comprehensive loss were:

| <i>In thousands</i> | December 31, | |
|--|---------------------|--------------------|
| | 2003 | 2002 |
| Foreign currency translation adjustment | \$ (3,525) | \$ (17,487) |
| Unrealized losses on derivatives designated and qualified as cash flow hedges, net of tax of \$(119) and \$(615) | (207) | (1,006) |
| Unrealized gains on other derivatives, net of tax of \$135 and \$0 | 235 | |
| Additional minimum pension liability, net of tax of \$(9,423) and \$(8,695) | (16,392) | (13,599) |
| Total accumulated other comprehensive loss | \$ (19,889) | \$ (32,092) |

15. OPERATING LEASES

The Company leases office and manufacturing facilities under operating leases with terms ranging from one to 15 years, excluding renewal options.

The Company has sold remanufactured locomotives to various financial institutions and leased them back under operating leases with terms from five to 20 years.

Total net rental expense charged to operations in 2003, 2002, and 2001 was \$6.9 million, \$6.2 million and \$5.7 million, respectively. Certain of the Company's equipment rental obligations under operating leases pertain to locomotives, which are subleased to customers under both short-term and long-term agreements. The amounts above are shown net of sublease rentals of \$2.8 million, \$2.8 million and \$2.8 million for the years 2003, 2002 and 2001, respectively.

Future minimum rental payments under operating leases with remaining noncancelable terms in excess of one year are as follows:

| <u><i>In thousands</i></u> | <u>Real Estate</u> | <u>Equipment</u> | <u>Sublease Rentals</u> | <u>Total</u> |
|----------------------------|------------------------|------------------|-----------------------------|--------------|
| 2004 | \$ 4,708 | \$ 4,846 | \$ (2,498) | \$ 7,056 |
| 2005 | 4,468 | 4,503 | (2,411) | 6,560 |
| 2006 | 4,415 | 4,135 | (2,347) | 6,203 |
| 2007 | 4,271 | 2,150 | (1,571) | 4,850 |
| 2008 | 5,259 | 2,132 | (1,455) | 5,936 |
| 2009 and after | 12,896 | | | 12,896 |

16. GUARANTEES

In 2001, the Company sold a small non-core operating unit to its management team. As part of the sale, Wabtec guaranteed approximately \$3 million of bank debt of the buyer, which was used for the purchase financing. In the event that the purchaser cannot repay or refinance the debt without a guarantee by Wabtec, the business would be returned to Wabtec. This debt is due in 2004. The Company has no reason to believe that this debt will not be repaid or refinanced.

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

| <u><i>In thousands</i></u> | For the year ended | |
|--------------------------------|---------------------------|-------------|
| | December 31, | |
| | <u>2003</u> | <u>2002</u> |
| Balance at beginning of period | \$ 17,407 | \$ 15,373 |
| Warranty expense | 10,489 | 17,625 |

| | | |
|--------------------------|-------------------|-------------------|
| Warranty payments | (14,589) | (15,591) |
| | <u> </u> | <u> </u> |
| Balance at end of period | \$ 13,307 | \$ 17,407 |
| | <u> </u> | <u> </u> |

17. STOCKHOLDERS AGREEMENTS

As of December 31, 2003 the approximate ownership interests in the Company's Common Stock are: management (12%), American Industrial Partners Capital Fund II, L.P. (2%), and all others including public shareholders (86%).

A Stockholders Agreement exists between the Company and American Industrial Partners that provides for, among other things, the composition of the Board of Directors as long as certain minimum stock ownership percentages are maintained, and rights to request the registration of the shares.

18. PREFERRED STOCK

The Company's authorized capital stock includes 1,000,000 shares of preferred stock. The Board of Directors has the authority to issue the preferred stock and to fix the designations, powers, preferences and rights of the shares of each such class or series, including dividend rates, conversion rights, voting rights, terms of redemption and liquidation preferences, without any further vote or action by the Company's shareholders. The rights and preferences of the preferred stock would be superior to those of the common stock. At December 31, 2003 and 2002 there was no preferred stock issued or outstanding.

19. COMMITMENTS AND CONTINGENCIES

The Company is subject to a variety of environmental laws and regulations governing discharges to air and water, the handling, storage and disposal of hazardous or solid waste materials and the remediation of contamination associated with releases of hazardous substances. The Company believes its operations currently comply in all material respects with all of the various environmental laws and regulations applicable to our business; however, there can be no assurance that environmental requirements will not change in the future or that we will not incur significant costs to comply with such requirements.

Under terms of the purchase agreement and related documents for the 1990 Acquisition, American Standard, Inc. (ASI) has indemnified the Company for certain items including, among other things, certain environmental claims the Company asserted prior to 2000. If ASI was unable to honor or meet these indemnifications, the Company would be responsible for such items. In the opinion of management, ASI currently has the ability to meet its indemnification obligations.

Actions have been filed against us and certain of our 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. 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 before we acquired American Standard, Inc. s (ASI) 50% interest in RFPC in 1990. We acquired the remaining interest in RFPC in 1992. These claims include a suit against RFPC by ASI seeking contribution and indemnity for asbestos claims brought against ASI that ASI alleges claim exposure to RFPC s product.

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. Neither we nor our affiliates have to date incurred material costs relating to these asbestos claims. 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 with certainty.

BOISE, IDAHO

The Company is subject to a RCRA Part B Closure Permit (the Permit) issued by the Environmental Protection Agency (EPA) and the Idaho Department of Health and Welfare, Division of Environmental Quality relating to the monitoring and treatment of groundwater contamination on, and adjacent to, the MotivePower Industries (Boise, Idaho) facility. In compliance with the Permit, the Company has completed the first phase of an accelerated plan for the treatment of contaminated groundwater, and continues onsite and offsite monitoring for hazardous constituents. The Company has accrued \$585,000 at December 31, 2003, the estimated remaining costs for remediation. The Company was in compliance with the Permit at December 31, 2003.

MOUNTAINTOP, PENNSYLVANIA

Foster Wheeler Energy Corporation (FWEC) the seller of the Mountaintop property to the predecessor of one of the Company s subsidiaries in 1989, agreed to indemnify the Company s predecessor and its successors and assigns against certain identified environmental liabilities for which FWEC executed a Consent Order Agreement with the Pennsylvania Department of Environmental Protection (PADEP) and EPA. On October 14, 2003, the Company executed a Consent Order and Agreement with PADEP pursuant to the PA Land Recycling and Environmental Remediation Standards Act (Act 2), entitling the Company to the liability protections afforded under Act 2 for the environmental contamination identified in the Agreement. Management believes that the Act 2 protection and the FWEC indemnification arrangement are enforceable for the

benefit of the Company. Management believes that this indemnification arrangement is enforceable for the benefit of the Company and that FWEC has the financial resources to honor its obligations under this indemnification arrangement.

MATTOON, ILLINOIS

Prior to the Company's acquisition of Young Radiator, Young agreed to clean up alleged contamination on a prior production site in Mattoon, Ill. The Company is in the process of remediating the site with the state of Illinois and now estimates the costs to remediate the site to be approximately \$251,000 which has been accrued at December 31, 2003.

RACINE, WISCONSIN

Young ceased manufacturing operations at its Racine facility in the early 1990s. Investigations prior to the acquisition of Young revealed some levels of contamination on the Racine property and the Company has begun remediation efforts. The Company has initiated a comprehensive site evaluation with the state of Wisconsin and believes this governing body is generally in agreement with the findings. The Company has accrued approximately \$259,000 at December 31, 2003 as its estimate of the remaining remediation costs.

GETS-GS

On November 3, 2000, the Company settled a suit brought against it in 1999 by GE-Harris Railway Electronics, L.L.C. and GE-Harris Railway Electronics Services, L.L.C. (collectively "GE-Harris"). On September 20, 2002, a motion in that lawsuit was filed by the successor to GE Harris, GE Transportation Services Global Signaling, L.L.C. ("GETS-GS"). The motion by GETS-GS contends that the Company is acting beyond authority granted in the parties' November 2000 settlement and license agreement and in contempt of the consent order that concluded the suit at that time. In support of its motion, GETS-GS points principally to sales and offers to sell certain railway brake equipment, including distributed power equipment, to Australian customers. GETS-GS is seeking substantial money damages and has claimed a significant business loss. A two day hearing was held on GETS-GS' motion in May 2003. The parties completed and filed all post-hearing papers on August 28, 2003. Barring a settlement agreement in the interim, the parties are awaiting the court's decision and opinion on the motion.

The Company has other contingent obligations relating to certain sales leaseback transactions, for locomotives that were assumed in connection with the MotivePower merger in 1999, for which reserves of \$5.8 million have been established.

From time to time the Company is involved in litigation relating to claims arising out of its operations in the ordinary course of business. As of the date hereof, the Company is involved in no litigation that the Company believes will have a material adverse effect on its financial condition, results of operations or liquidity.

20. SEGMENT INFORMATION

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

Freight Group manufactures products and provides services geared to the production and operation of freight cars and locomotives, including braking control equipment, engines, on-board electronic components and train coupler equipment. Revenues are derived from OEM sales and locomotive overhauls, aftermarket sales and from freight car repairs and services. All of the assets sold to GETS were part of the Freight Group.

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

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

Segment financial information for 2003 is as follows:

| <u>In thousands</u> | <u>Freight Group</u> | <u>Transit Group</u> | <u>Corporate Activities</u> | <u>Merger and Restructuring</u> | <u>Total</u> |
|--|--------------------------|--------------------------|---------------------------------|-------------------------------------|-------------------|
| Sales to external customers | \$ 522,279 | \$ 195,645 | | | \$ 717,924 |
| Intersegment sales/(elimination) | 8,998 | 686 | (9,684) | | |
| Total sales | \$ 531,277 | \$ 196,331 | \$ (9,684) | | \$ 717,924 |
| Income (loss) from operations | \$ 76,042 | \$ 198 | \$ (24,531) | | \$ 51,709 |
| Interest expense and other | | | (16,667) | | (16,667) |
| Income (loss) from continuing operations before income taxes and cumulative effect of accounting change | \$ 76,042 | \$ 198 | \$ (41,198) | | \$ 35,042 |
| Depreciation and amortization | 17,897 | 5,178 | 2,209 | | 25,284 |
| Capital expenditures | 12,097 | 1,581 | 3,792 | | 17,470 |
| Segment assets | 418,064 | 150,435 | 87,806 | | 656,305 |

Segment financial information for 2002 is as follows:

| <u>In thousands</u> | <u>Freight Group</u> | <u>Transit Group</u> | <u>Corporate Activities</u> | <u>Merger and Restructuring</u> | <u>Total</u> |
|--|--------------------------|--------------------------|---------------------------------|-------------------------------------|-------------------|
| Sales to external customers | \$ 443,443 | \$ 252,752 | | | \$ 696,195 |
| Intersegment sales/(elimination) | 8,849 | 567 | (9,416) | | |
| Total sales | \$ 452,292 | \$ 253,319 | \$ (9,416) | | \$ 696,195 |
| Income (loss) from operations | \$ 48,186 | \$ 22,237 | \$ (22,889) | | \$ 47,534 |
| Interest expense and other | | | (23,630) | | (23,630) |
| Income (loss) from continuing operations before income taxes and cumulative effect of accounting change | \$ 48,186 | \$ 22,237 | \$ (46,519) | | \$ 23,904 |
| Depreciation and amortization | 17,166 | 5,761 | 2,586 | | 25,513 |
| Capital expenditures | 9,134 | 3,757 | 1,246 | | 14,137 |
| Segment assets | 375,032 | 142,764 | 71,069 | | 588,865 |

Segment financial information for 2001 is as follows:

| <u>In thousands</u> | <u>Freight Group</u> | <u>Transit Group</u> | <u>Corporate Activities</u> | <u>Merger and Restructuring</u> | <u>Total</u> |
|---------------------|--------------------------|--------------------------|---------------------------------|-------------------------------------|--------------|
|---------------------|--------------------------|--------------------------|---------------------------------|-------------------------------------|--------------|

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| | | | | | |
|---|------------|------------|-------------|------------|------------|
| Sales to external customers | \$ 490,261 | \$ 293,437 | | | \$ 783,698 |
| Intersegment sales/(elimination) | 10,160 | 788 | (10,948) | | |
| Total sales | \$ 500,421 | \$ 294,225 | \$ (10,948) | | \$ 783,698 |
| Income (loss) from operations | \$ 58,989 | \$ 32,390 | \$ (33,598) | \$ (3,723) | \$ 54,058 |
| Interest expense and other | | | (35,631) | | (35,631) |
| Income (loss) from continuing operations before income taxes and cumulative effect of accounting change | \$ 58,989 | \$ 32,390 | \$ (69,229) | \$ (3,723) | \$ 18,427 |
| Depreciation and amortization | 23,234 | 7,337 | 2,490 | | 33,061 |
| Capital expenditures | 14,048 | 4,469 | 2,157 | | 20,674 |
| Segment assets | 477,983 | 175,028 | 76,941 | | 729,952 |

In 2001, \$530,000 of the merger and restructuring costs related to the Freight Group, and \$2 million related to the Transit Group.

The following geographic area data as of and for the years ended December 31, 2003, 2002 and 2001, respectively, includes net sales based on product shipment destination and long-lived assets, which consist of plant, property and equipment, net of depreciation, resident in their respective countries:

| <i>In thousands</i> | Net Sales | | | Long-Lived Assets | | |
|---------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| | 2003 | 2002 | 2001 | 2003 | 2002 | 2001 |
| United States | \$ 497,579 | \$ 525,724 | \$ 582,655 | \$ 99,091 | \$ 99,292 | \$ 115,583 |
| Canada | 61,770 | 50,035 | 73,177 | 31,786 | 27,889 | 32,963 |
| Mexico | 10,225 | 11,487 | 8,693 | 10,473 | 10,979 | 10,584 |
| Other international | 148,350 | 108,949 | 119,173 | 12,489 | 10,432 | 8,565 |
| Total | \$ 717,924 | \$ 696,195 | \$ 783,698 | \$ 153,839 | \$ 148,592 | \$ 167,695 |

Export sales from the Company's United States operations were \$59.2 million, \$61.9 million and \$90.3 million for the years ending December 31, 2003, 2002 and 2001, respectively. The following data reflects income (loss) from operations, including merger and restructuring related charges by major geographic area, attributed to the Company's operations within each of the following countries or regions for the years ended December 31, 2003, 2002 and 2001, respectively:

| <i>In thousands</i> | Income (Loss) from Operations | | |
|---------------------|-------------------------------|------------------|------------------|
| | 2003 | 2002 | 2001 |
| United States | \$ 44,192 | \$ 34,554 | \$ 41,007 |
| Canada | (6,385) | 496 | 6,412 |
| Mexico | 166 | (325) | (2,467) |
| Other international | 13,736 | 12,809 | 9,106 |
| Total | \$ 51,709 | \$ 47,534 | \$ 54,058 |

21. FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair values of the Company's financial instruments approximate their related carrying values, except for the following:

| <i>In thousands</i> | 2003 | | 2002 | |
|---------------------|-------------|------------|-------------|------------|
| | Carry Value | Fair Value | Carry Value | Fair Value |
| | | | | |

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| | | | | |
|--|----------|----------|------------|---------|
| Interest rate swaps | \$ (377) | \$ (377) | \$ (1,756) | (1,756) |
| Foreign exchange hedges and option contracts | 235 | 235 | | |
| 6.875% senior notes | 150,000 | 155,000 | | |

The fair value of the Company's interest rate swaps (see Note 9), foreign exchange hedges and option contracts and senior notes were based on dealer quotes and represent the estimated amount the Company would pay to the counterparty to terminate the agreements.

22. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

| | First | Second | Third | Fourth |
|--|------------|------------|------------|------------|
| <i>In thousands, except per share data</i> | Quarter | Quarter | Quarter | Quarter |
| 2003 | | | | |
| Net sales | \$ 169,523 | \$ 174,856 | \$ 167,189 | \$ 206,356 |
| Gross profit | 45,276 | 47,562 | 43,425 | 53,187 |
| Operating income | 12,301 | 13,842 | 10,647 | 14,919 |
| Income from continuing operations before taxes | 8,766 | 8,771 | 8,740 | 8,765 |
| Income (loss) from discontinued operations (net of tax) | 117 | (44) | 53 | 325 |
| Net income | 5,683 | 5,526 | 5,603 | 5,891 |
| Basic earnings from continuing operations per common share | \$ 0.13 | \$ 0.13 | \$ 0.13 | \$ 0.12 |
| Diluted earnings from continuing operations per common share | \$ 0.13 | \$ 0.13 | \$ 0.13 | \$ 0.12 |
| 2002 | | | | |
| Net sales | \$ 177,325 | \$ 179,808 | \$ 161,422 | \$ 177,640 |
| Gross profit | 44,780 | 45,356 | 43,284 | 46,051 |
| Operating income | 10,467 | 13,300 | 11,170 | 12,597 |
| Income from continuing operations before taxes | 4,044 | 7,329 | 5,910 | 6,621 |
| Income (loss) from discontinued operations (net of tax) | (405) | 57 | 48 | 174 |
| Net (loss) income | (59,440) | 4,821 | 3,890 | 5,250 |
| Basic earnings from continuing operations per common share | \$ 0.06 | \$ 0.11 | \$ 0.09 | \$ 0.12 |
| Diluted earnings from continuing operations per common share | \$ 0.06 | \$ 0.11 | \$ 0.09 | \$ 0.12 |

Earnings per share for 2002 are different than the sum of the quarterly earnings per share due to rounding.

The Company recorded a cumulative effect of accounting change for goodwill, net of tax, of \$61.7 million, or \$1.41 in the first quarter of 2002. In the fourth quarter of 2002, the Company recorded a \$772,000, or \$0.02, per diluted share tax benefit due to research and development credits and the utilization of foreign tax credits. Also in the fourth quarter of 2002, the Company's vacation policy was changed so that employees that leave the Company are entitled to a pro rata portion of their vacation for that year instead of their entire vacation for the year. This change resulted in income of \$789,000, net of tax, or \$0.02 per diluted share.

23. RESTRUCTURING CHARGE

In 2001, the Company completed a merger and restructuring plan with charges totaling \$71 million pre-tax, with approximately \$2 million of the costs expensed in 2001, \$20 million in 2000 and \$49 million in 1999. The plan involved the elimination of duplicate facilities and excess capacity, operational realignment and related workforce reductions, and the evaluation of certain assets as to their perceived ongoing benefit to the Company.

As of December 31, 2003, \$86,000 of the merger and restructuring charge was still remaining as accrued on the balance sheet as part of other accrued liabilities. The table below identifies the significant components of the charge and reflects the accrual balance at that date.

| <i>In thousands</i> | Lease Impairments | Total |
|------------------------------------|----------------------|--------|
| Beginning balance, January 1, 2003 | \$ 647 | \$ 647 |

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| | | |
|------------------------------|------------|------------|
| Amounts paid in 2003 | <u>561</u> | <u>561</u> |
| Balance at December 31, 2003 | <u>86</u> | <u>86</u> |

The lease impairment charges are associated with the Company's closing of a plant and the consolidation of the corporate headquarters.

WESTINGHOUSE AIR BRAKE TECHNOLOGIES CORPORATION

VALUATION AND QUALIFYING ACCOUNTS

For each of the three years ended December 31

| <i>In thousands</i> | Balance at beginning of period | Charged/ (credited) to expense | Charged to other accounts ⁽¹⁾ | Deductions from reserves ⁽²⁾ | Balance at end of period |
|----------------------------------|--------------------------------------|--------------------------------------|--|---|--------------------------------|
| 2003 | | | | | |
| Warranty and overhaul reserves | \$ 17,407 | \$ 10,489 | \$ | \$ 14,589 | \$ 13,307 |
| Allowance for doubtful accounts | 4,647 | 1,576 | | 1,771 | 4,452 |
| Valuation allowance - taxes | 14,566 | | 3,921 | | 18,487 |
| Inventory reserves | 12,408 | 5,326 | | 1,331 | 16,403 |
| Merger and restructuring reserve | 647 | | | 561 | 86 |
| 2002 | | | | | |
| Warranty and overhaul reserves | \$ 15,373 | \$ 17,625 | \$ | \$ 15,591 | \$ 17,407 |
| Allowance for doubtful accounts | 2,294 | 2,923 | | 570 | 4,647 |
| Valuation allowance- taxes | 8,641 | | 5,925 | | 14,566 |
| Inventory reserves | 13,228 | 3,802 | | 4,622 | 12,408 |
| Merger and restructuring reserve | 3,152 | | | 2,505 | 647 |
| 2001 | | | | | |
| Warranty and overhaul reserves | \$ 23,482 | \$ 19,821 | \$ (6,658) | \$ 21,272 | \$ 15,373 |
| Allowance for doubtful accounts | 3,949 | 2,151 | (1,287) | 2,519 | 2,294 |
| Valuation allowance- taxes | 8,641 | | | | 8,641 |
| Inventory reserves | 17,309 | 8,569 | (3,689) | 8,961 | 13,228 |
| Merger and restructuring reserve | 6,257 | 3,723 | | 6,828 | 3,152 |

(1) Reserves of acquired/(sold) companies and valuation allowances for state and foreign deferred tax assets

(2) Actual disbursements and/or charges

EXHIBITS

| Exhibits | Filing Method | |
|----------|---|----|
| 2.1 | Amended and Restated Agreement and Plan of Merger, as amended (originally included as Annex A to the Joint Proxy Statement/Prospectus) | 8 |
| 3.1 | Restated Certificate of Incorporation of the Company dated January 30, 1995, as amended March 30, 1995 | 2 |
| 3.3 | Amended and Restated By-Laws of the Company, effective November 19, 1999 | 8 |
| 4.1(a) | Indenture with the Bank of New York as Trustee dated as of August 6, 2003 | 15 |
| 4.1(b) | Resolutions Adopted July 23, 2003 by the Board of Directors establishing the terms of the offering of up to \$150,000,000 aggregate principal amount of 6.875% Notes due 2013 | 15 |
| 4.2 | Purchase Agreement, dated July 23, 2003, by and between the Company and the initial purchasers | 15 |
| 4.3 | Exchange and Registration Rights Agreement, dated August 6, 2003 | 15 |
| 10.1 | MotivePower Stock Option Agreement (originally included as Annex B to the Joint Proxy Statement/Prospectus) | 8 |
| 10.2 | Westinghouse Air Brake Stock Option Agreement (originally included as Annex C to the Joint Proxy Statement/Prospectus) | 8 |
| 10.3 | Voting Agreement dated as of September 26, 1999 among William E. Kassling, Robert J. Brooks, Harvard Private Capital Holdings, Inc. Vestar Equity Partners, L.P. and MotivePower Industries, Inc. (originally included as Annex D to the Joint Proxy Statement/Prospectus) | 8 |
| 10.9 | Amended and Restated Refinancing Credit Agreement dated as of November 19, 1999 among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York (Schedules and Exhibits omitted) | 9 |
| 10.10 | Amended and Restated Stockholders Agreement dated as of March 5, 1997 among the RAC Voting Trust (Voting Trust), Vestar Equity Partners, L.P. (Vestar Equity), Harvard Private Capital Holdings, Inc. (Harvard), American Industrial Partners Capital Fund II, L.P. (AIP) and the Company | 5 |
| 10.12 | Indemnification Agreement dated January 31, 1995 between the Company and the Voting Trust Trustees | 2 |
| 10.13 | Agreement of Sale and Purchase of the North American Operations of the Railway Products Group, an operating division of American Standard Inc., dated as of 1990 between Rail Acquisition Corp. and American Standard Inc. (only provisions on indemnification are reproduced) | 2 |
| 10.14 | Letter Agreement (undated) between the Company and American Standard Inc. on environmental costs and sharing | 2 |
| 10.15 | Purchase Agreement dated as of June 17, 1992 among the Company, Schuller International, Inc., Manville Corporation and European Overseas Corporation (only provisions on indemnification are reproduced) | 2 |
| 10.16 | Asset Purchase Agreement dated as of January 23, 1995 among the Company, Pulse Acquisition Corporation, Pulse Electronics, Inc., Pulse Embedded Computer Systems, Inc. and the Pulse Shareholders (Schedules and Exhibits omitted) | 2 |
| 10.17 | License Agreement dated as of December 31, 1993 between SAB WABCO Holdings B.V. and the Company | 2 |
| 10.18 | Letter Agreement dated as of January 19, 1995 between the Company and Vestar Capital Partners, Inc. | 2 |
| 10.19 | Westinghouse Air Brake Company 1995 Stock Incentive Plan, as amended | 7 |
| 10.20 | | 9 |

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| | | |
|-------|---|---|
| | Westinghouse Air Brake Company 1995 Non-Employee Directors Fee and Stock Option Plan, as amended | |
| 10.22 | Letter Agreement dated as of January 1, 1995 between the Company and Vestar Capital Partners, Inc. | 2 |
| 10.23 | Form of Indemnification Agreement between the Company and Authorized Representatives | 2 |
| 10.27 | Amendment No. 1 to Amended and Restated Stockholders Agreement dated as of March 5, 1997 among the Voting Trust, Vestar, Harvard, AIP and the Company | 5 |
| 10.28 | Common Stock Registration Rights Agreement dated as of March 5, 1997 among the Company, Harvard, AIP and the Voting Trust | 5 |

| | | |
|-------|---|----|
| 10.29 | 1998 Employee Stock Purchase Plan | 7 |
| 10.32 | Westinghouse Air Brake Technologies Corporation 2000 Stock Incentive Plan | 10 |
| 10.33 | Amendment No. 1, dated as of November 16, 2000, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999 among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 11 |
| 10.34 | Amendment No. 2, dated as of March 30, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Chase Manhattan Bank as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.35 | Amendment No. 3, dated as of July 18, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association and ABN AMRO Bank N.V. as bookrunner and co-syndication agent, The Bank of New York, as co-syndication agent, The Chase Manhattan Bank as administrative agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.36 | Amendment No. 4, dated as of September 17, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, The Chase Manhattan Bank as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, LaSalle Bank National Association, The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |
| 10.37 | Amendment No. 5, dated as of November 14, 2001, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, JP Morgan Chase Bank (formerly known as The Chase Manhattan Bank) as administrative agent, The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 (Exhibits omitted) | 13 |

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| 10.38 | Amendment No. 6, dated as of November 13, 2002, by and among the Company and the Guarantors from Time to Time Party Thereto, and the Banks From Time to Time Party Thereto, and LaSalle Bank National Association as bookrunner and co-syndication agent, JP Morgan Chase Bank as administrative agent, and The Bank of New York, as co-syndication agent, Mellon Bank, N.A., as documentation agent, LaSalle Bank National Association, as an issuing bank, ABN AMRO Bank N.V., as an issuing bank, and The Chase Manhattan Bank USA, N.A., (successor in interest to Chase Manhattan Bank Delaware), as an issuing bank, to the Amended and Restated Refinancing Credit Agreement, dated as of November 19, 1999, as amended, among the Company, various financial institutions, ABN AMRO Bank N.V., The Chase Manhattan Bank, and The Bank of New York which was filed as Exhibit 10.9 to the Company's Annual Report on Form 10-K for the period ended December 31, 1999 | 14 |
| 10.39 | Asset Purchase Agreement, by and between General Electric Company, through its GE Transportation Systems business and Westinghouse Air Brake Technologies Corporation, dated as of July 24, 2001 | 12 |
| 10.40 | Refinancing Credit Agreement by and among the Company, the Guarantors, various lenders, LaSalle Bank National Association, JP Morgan Chase Bank, The Bank of New York, Citizens Bank of Pennsylvania, National City Bank of Pennsylvania, The Bank of Nova Scotia, Bank of Tokyo-Mitsubishi Trust Company and PNC Bank, National Association dated January 12, 2004 | 1 |
| 21 | List of subsidiaries of the Company | 1 |
| 23.1 | Consent of Ernst & Young LLP | 1 |
| 23.2 | Information Regarding Consent of Arthur Andersen LLP | 1 |
| 31.1 | Rule 13a-14(a)/15d-14(a) Certifications | 1 |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certifications | 1 |
| 32.1 | Section 1350 Certifications | 1 |
| 32.2 | Section 1350 Certifications | 1 |
| 99.1 | Annual Report on Form 11-K for the year ended December 31, 2002 of the Westinghouse Air Brake Technologies Corporation Savings Plan | 1 |
| 99.2 | Annual Report on Form 11-K for the year ended December 31, 2003 of the Westinghouse Air Brake Technologies Corporation Savings Plan for Hourly Employees | 1 |

1 Filed herewith.

2 Filed as an exhibit to the Company's Registration Statement on Form S-1 (No. 33-90866).

3 Filed as an exhibit to the Company's Current Report on Form 8-K, dated October 3, 1996.

4 Filed as an exhibit to the Company's Registration Statement on Form S-8 (No. 333-39159).

5 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1997.

6 Filed as an exhibit to the Company's Current Report on Form 8-K, dated October 5, 1998.

7 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1998.

8 Filed as part of the Company's Registration Statement on Form S-4 (No. 333-88903).

9 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 1999.

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- 10 Filed as an exhibit to the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2000.
- 11 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2000.
- 12 Filed as an exhibit to the Company's Current Report on Form 8-K, dated November 13, 2001.
- 13 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2001.
- 14 Filed as an exhibit to the Company's Annual Report on Form 10-K for the period ended December 31, 2002.
- 15 Filed as an exhibit to the Company's Registration Statement on Form S-4 (No. 333-110600).