UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

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

☑ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
for the fiscal year ended February 23, 2007

or

☐ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from ___________ to ___________.

Commission File Number 1-10655

ENVIRONMENTAL TECTONICS CORPORATION

Pennsylvania	23-1714256
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

County Line Industrial Park
Southampton, Pennsylvania 18966
(Address of principal executive offices, Zip Code)

Registrant's telephone number, including area code (215) 355-9100
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $.05 per share	American Stock Exchange

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in rule 405 of the Securities Act. Yes ☐ No ☑

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes ☐ No ☑

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large Accelerated Filer ☐ Accelerated Filer ☐ Non-accelerated Filer ☑

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

As of August 25, 2006, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $39,666,000 based upon the closing sale price of the registrant's common stock on the American Stock Exchange of $6.03 on such date. See footnote (1) below.

As of May 11, 2007, there were 9,028,469 shares of the registrant's common stock issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE. Portions of registrant's 2007 Annual Report to Stockholders are incorporated by reference in Part II, Items 5, 6, 7, and 8.

Index to Exhibits appears after page 31 of this Report.

(1) The information provided is not an admission that any person whose holdings are excluded from the figure is not an affiliate or that any person whose holdings are included is an affiliate and any such admission is hereby disclaimed. The information provided is solely for record keeping purposes of the Securities and Exchange Commission.

ENVIRONMENTAL TECTONICS CORPORATION
ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED
FEBRUARY 23, 2007

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When used in this Annual Report on Form 10-K, except where the context otherwise requires, the terms “we”, “us”, “our”, “ETC” and the “Company” refer to Environmental Tectonics Corporation.

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are based on ETC's current expectations and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about ETC's and its subsidiaries that may cause actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements.

These forward-looking statements include statements with respect to ETC's vision, mission, strategies, goals, beliefs, plans, objectives, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance and business of ETC, including but not limited to, (i) projections of revenue, costs of raw materials, income or loss, earnings or loss per share, capital expenditures, growth prospects, dividends, capital structure, other financial items and the effects of currency fluctuations, (ii) statements of plans and objectives of ETC or its management or Board of Directors, including the introduction of new products, or estimates or predictions of actions of customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, (iv) statements of assumptions and other statements about ETC or its business, (v) statements made about the possible outcomes of litigation involving ETC, and (vi) statements preceded by, followed by or that include the words "may", "could", "should", "looking forward", "would", "believe", "expect", "anticipate", "estimate", "intend", "plan", or the negative of such terms or similar expressions. These forward-looking statements involve risks and uncertainties which are subject to change based on various important factors. Some of these risks and uncertainties, in whole or in part, are beyond ETC's control. Factors that might cause or contribute to such a material difference include, but are not limited to, those discussed in this Annual Report on Form 10-K, in the section entitled "Risks Particular to Our Business." Shareholders are urged to review these risks carefully prior to making an investment in the ETC's common stock.

The Company cautions that the foregoing list of important factors is not exclusive. ETC does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of ETC.

References to fiscal 2007 or the 2007 fiscal year are references to the year ended February 23, 2007. References to fiscal 2008 or the 2008 fiscal year are references to the year ending February 29, 2008.

PART I

Item 1. Business

We were incorporated in 1969 in Pennsylvania and are principally engaged in the design, manufacture and sale of software driven products and services used to recreate and monitor the physiological effects of motion on humans and equipment and to control, modify, simulate and measure environmental conditions. These products include aircrew training systems (aeromedical, tactical combat and general), disaster management training systems and services, entertainment products, sterilizers (steam and gas), environmental testing products and hyperbaric chambers and other products that involve similar manufacturing techniques and engineering technologies.

Segments

We operate in two primary business segments, the Training Services Group ("TSG") (formerly Aircrew Training Systems (ATS)) and the Control Systems Group ("CSG") (formerly the Industrial Group (IG)).

Training Services Group. This segment includes three primary product groups: aircrew training devices and services, disaster management training and systems, and entertainment products.

Integrated Aircrew Training. Aircrew training is performed in our National Aerospace Training and Research (NASTAR) Center. This center, set to open in fiscal 2008, is an integrated pilot training center offering a complete range of aviation training and research support for military jet pilots and civil aviation as well as space travel and tourism. The NASTAR Center houses state of the art pilot training equipment including the ATFS-400 Centrifuge, GYROLAB GL-2000 Advanced Spatial Disorientation Trainer, Hypobaric Altitude Chamber, an Ejection Seat Trainer, and Night Vision and Night Vision Goggle Training System.

Aircrew Training Systems. We design, develop and manufacture a full range of pilot training devices. Aircrew training devices are used for medical research, advanced tactical and physiological flight training, and for the indoctrination and testing of military and commercial pilots. The major devices that we sell in this business segment are military and commercial flight simulators, night vision trainers, water survival training equipment, disorientation training equipment, human centrifuges, ejection seat trainers and vehicle simulators. We provide operational and maintenance services for installed equipment that we manufacture as well as for equipment produced by others.

Disaster Management Training and Systems. Our Disaster Management Simulation line includes real-

time interactive training and systems that provide instruction on various disaster situations.

Entertainment Products. Our entertainment products consist of motion-based simulation rides and other products for the education and amusement industries.

The Training Services Group segment generated 53%, 60% and 60% of our consolidated revenues for the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005, respectively.

Control Systems Group. This segment includes three primary product lines: sterilizers, environmental control systems and other products, and hyperbarics.

Sterilizers. We manufacture steam and gas sterilizers for various industrial and pharmaceutical applications. We concentrate on marketing larger custom-designed sterilizers to the pharmaceutical and medical device industries.

Environmental Control Systems and Other Products. Our environmental systems business consists of the design and fabrication of sampling and analysis systems, and test equipment and systems. The simulation systems generally consist of an enclosed chamber with instrumentation and equipment which enable the customer to control and modify environmental factors such as temperature, pressure, humidity, wind velocity and gas content to produce desired conditions. These products include controlled air systems for automotive companies and environmental chambers for HVAC and other applications.

Hyperbarics. Our hyperbaric product line includes monoplace (single person) and multiplace (multiple persons) chambers for high altitude training, decompression and wound care applications.

The Control Systems Group generated 47%, 40% and 40% of our consolidated revenues for the years ended February 23, 2007, February 24, 2006 and February 25, 2005, respectively.

We also provide control upgrades, maintenance and repair services and spare parts for equipment which we manufacture and for equipment made by other manufacturers.

For a more complete description of financial information regarding our business segments, see “Note 11. Business Segment Information” to our consolidated financial statements in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

Marketing

We currently market our products and services primarily through our sales offices and employees. At February 23, 2007, approximately 29 employees were committed to sales and marketing functions. We use branch offices in England, Turkey, Egypt, Singapore, the United Arab Emirates, Malaysia and Japan as well as the services of approximately 100 independent sales organizations in seeking foreign orders for our products.

Product Development

We are continually developing new products and improving existing products in response to inquiries from customers and in response to our determination that particular products should be produced or significantly improved. Although we do not have a separate research and development group, we have several technical personnel whose main activity is the development and integration of new technologies into our existing products. These personnel include the Vice President Engineering Manager and the Vice President of Development whose additional responsibility is the introduction of product extensions and new applications of existing technology.

Within the Training Services Group segment, product development emphasizes additional functionality and fidelity, enhancing control systems and software graphics and exploring commercial possibilities. Our product development efforts are as follows:

Tactical Flight Combat and G-force / Disorientation Trainers.

In response to the ongoing market budgetary constraints for pilot G-force training and spatial disorientation, in 2004 we began incorporating tactical combat flight capabilities into our centrifuge technology. Dubbed the Authentic Tactical Fighting System (ATFS), this product was the first fully “flyable” centrifuge-based tactical maneuvering ground based simulator. This technology allows a fighter pilot to practice tactical air combat maneuvers such as dodging enemy missiles, ground fire and aircraft obstacles while experiencing the real life environment of a high G-force fighter aircraft. These flight trainers provide a low cost and extremely less risky alternative to actual air flight. We continued development of this technology through fiscal 2007 including incorporating some of this functionality into our GYROLAB products as we received significant orders from the Japanese Defense Agency for a GL-4000 and from a Middle Eastern customer for a GL-1500.

Advanced Disaster Management Simulator (ADMS) .

During fiscal 2007, our simulation line continued to expand its influence in the disaster management arena through our completion of the largest disaster management simulation center at the Korean National Fire Service Academy (KNFSA). The KNFSA ADMS system is being used to provide advanced training for all Korean fire service officers in low and high-rise internal structural firefighting, industrial and hazardous material fires, major road traffic accidents, urban search and rescue, and mountain wildfires. This system was installed in Cheonan, South Korea. With 20 networked training stations this is the largest ADMS installation to date.

The high-fidelity virtual environment created for the KNFSA encompasses nearly 200 square miles and features the crowded urban city regions and mountainous rural areas uniquely representative of Korea. Given that the dense and heavily populated Korean cities make it especially difficult to realistically train for massive incidents or natural disasters, KNFSA turned to ETC for simulation-based training. The KNFSA environment also features suburban residential areas and a commercial/industrial area. The ADMS Scenario Generator allows KNFSA to develop an unlimited number of training scenarios, from small, simple incidents to major mass-casualty disasters.

Domestically, the division continued work on a contract with the Pennsylvania Southeast Region Counter-Terrorism Task Force (CTTF) to provide an ADMS-TEAM training system.

We will continue to enhance product applications by adding additional software objects and increasing interactivity between the various disaster scenarios.

Subsidiaries

We presently have four operating subsidiaries. Entertainment Technology Corporation, our wholly owned subsidiary, is a Pennsylvania corporation that focuses on the development, manufacturing and distribution of our entertainment products. ETC-PZL Aerospace Industries, our 95%-owned subsidiary, is a Polish corporation that manufactures simulators. ETC-Europe, our 99%-owned subsidiary, is a United Kingdom corporation that focuses on generating international sales. NASTAR Center LLC is our wholly owned Delaware subsidiary which houses our NASTAR Center and all its activities. ETC-Delaware, our wholly-owned subsidiary, is a Delaware corporation that serves as a holding company.

Suppliers

The components being used in the assembly of systems and the parts used to manufacture our products are purchased from equipment manufacturers, electronics supply firms and others. Historically, we have had no difficulty in obtaining supplies. Further, all raw materials, parts, components and other supplies which we use to manufacture our products can be obtained at competitive prices from alternate sources should existing sources of supply become unavailable.

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Patents and Trademarks

We presently hold the following patents which we deem significant to our operations:

Patent Number	Title	Expiration Date
5,051,094	"G-Force Trainer"	9/24/08
6,818,178 B2	"Method for High Vacuum Sterilization of Closures"	1/15/23

We also hold a trademark on our logo, ETC®, as well as on the following products:

BARA-MED®	Medical Hyperbaric Chamber
DATAPRINT®	Digital Printer for Sterilizers
ETC®	Logo for Environmental Tectonics Corporation
GAT-II®	General Aviation Trainer
G-LAB®	Human Centrifuge/USAF Type
GYROLAB®	Spatial Disorientation Device
MRC Monster Roll Cage®	Interactive Simulator in the Nature of an Amusement Ride Machine that incorporates Virtual Reality Effects
THE RIDE WORKS®	(Facility for) Manufacture of Amusement and Entertainment Rides to the order and specification of others.

ETC's Unregistered (™) (SM) Trademark / Service Marks are:

ADMS™	Advanced Disaster Management Simulator
ATFS™	Authentic Tactical Fighting System
Authentic Tactical Fighting System ™	Authentic Tactical Fighting System
BARA-LAB™	Hyperbaric Chamber (other than medical)
BARA•PRESS	Hyperbaric Chamber Software
BIG MAC™	Entertainment ride based on a multi-armed Centrifuge Device
CAS™	Conditioned Air Supply
DMI™	Disaster Management Institute
EAGLE-VISION™	Visual Performance/Procedures Trainer
EPC™	Engine Pressure Controller/Environmental System
ETC™	ETC Biomedical Systems (***Stylized "ETC" with caduceus.***)
ETC™	Entertainment Technology Corporation (***Stylized "ETC" and name in color***)
G-FET™	Human Centrifuge (U.S. Navy type)
G-FET-II™	Human Centrifuge (Malaysian Air Force type)

G-MAS™	Missile Avoidance System (Centrifuge feature)
G-POINTING™	Motion control algorithm feature; namely, a feature of Flight Simulators that duplicates G-force effects experienced during tactical flight in Class 9.
GRAPH MASTER PROGRAMMER™	Industrial Sterilizer Control
GUARDIAN MONITORING PACKAGE™	GMP features for Sterilizers
GYRO-1™	Multi-purpose basic Instrument Flight Trainer
GYRO-SAT™	Situational Awareness Trainer (feature of a Gyrolab)
GYROSIM™	Gyrolab as a Simulator
LANE MASTER™	Automobile Emissions Analyzer
MAC™	Entertainment Ride based on a Multi-Armed Centrifuge Device
NASTAR℠ CENTER	The National Aerospace Training & Research Center (Standard Word Mark)
OASIS™	Software-driven tool to build Test and Training Systems and scoring them; curriculum development, capability assessment, etc.
ProFlyer™	Commercial Flight and Navigational Procedures Trainer meeting European regulations for civilian pilot training and certification
PRO-GENESIS™	Control Unit/column for Sterilizers
ProTrainer™	Commercial Instrument Procedures Trainer meeting FAA's PCATD requirements
SENTRY 84™	Automobile Emissions Analyzer
SMOOTH RIDE™	Computer Control Profile for Hyperbaric Chambers
TACModule™	Tactical Aircraft Configuration Module
TNET ™ and/or TRAINING NET™	Computer Software for training emergency personnel in firefighting, disaster management, etc.
TESS™	Total Emissions Suppression System, EtO Sterilizer
Thrills Without Ills™	Describing ETC's entertainment rides, particularly those utilizing ETC's Human Centrifuge Technology, which precludes motion sickness commonly associated with motion-based entertainment rides.
VPT-1000™	Visual Procedures Trainer

Customers

In the current fiscal year and throughout most of our history, we have made a substantial portion of our sales to a small number of customers that vary within any given fiscal year. We do not depend upon repeat orders from these same customers. We sell our aircrew training systems principally to U.S. and foreign governmental agencies. We sell sterilizers and environmental systems to commercial and governmental entities worldwide.

In fiscal 2007 one customer represented individually 10% or more of total sales, Jupitor (Japan), which generated $3,365,000 or 19.3% of total sales. International sales totaling at least $500,000 per country were made to customers in Japan, Australia and Pakistan. Open orders for one international and one domestic customer represented 43.9% of our backlog at February 23, 2007. We do not have any relationship with these customers other than as customers. We expect to continue to conduct business with these customers in fiscal 2008, albeit at a much reduced level.

Foreign and Domestic Operations and Export Sales

During the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005, approximately $586,000 (3%), $2,586,000 (10%) and $2,904,000 (10%), respectively, of our net revenues were attributable to contracts with agencies of the U.S. Government or with other customers who had prime contracts with agencies of the U.S. Government.

During the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005, $10,821,000 (62%), $13,343,000 (53%) and $12,912,000 (47%), respectively, of our net revenues were attributable to export sales, including those in our foreign subsidiaries. Our customers' obligations to us with regards to export sales are normally secured by irrevocable letters of credit based on the creditworthiness of the customer and the geographic area of the world in which they are located.

During the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005, $6,012,000 (35%), $9,140,000 (37%) and $11,998,000 (43%), respectively, of our net revenues were attributable to domestic sales to customers other than the U.S. government.

See "Note 11. Business Segment Information" to our consolidated financial statements in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

We do not believe that the distribution of our sales between foreign and domestic sales for any particular period is necessarily indicative of the distribution expected for any other period.

We derive a large portion of our sales from long-term contracts requiring more than one year to complete. We account for sales under long-term contracts on the percentage of completion basis. See the section Critical Accounting Policies in the Management's Discussion and Analysis of Financial Condition and Results of Operations and "Note 3. Summary of Significant Accounting Policies" to our consolidated financial statements in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

Our U.S. Government contracts contain standard terms permitting termination for the convenience of the U.S. Government. In the event of termination of a government contract, we are entitled to receive reimbursement on the basis of work completed (cost incurred plus a reasonable profit). We customarily record the amounts that we anticipate to be recovered from termination claims in income as soon as those amounts can be reasonably determined rather than at the time of final settlement. All costs applicable to a termination claim are charged as an offsetting expense concurrently with the recognition of income from the claim.

Manufacturing Facilities

Our manufacturing facility is located on a five-acre site in Southampton, PA, northwest of Philadelphia, PA. We have approximately 85,000 square feet devoted to manufacturing, assembly and testing. We have two centrifuge bays with specially designed foundations for testing human centrifuges and other centrifuge-technology-based simulators and amusement rides. ETC is ISO 9001-2000 certified.

Backlog

Our sales backlog at February 23, 2007 and February 24, 2006, for work to be performed and revenue to be recognized under written agreements after such dates, was $13,564,000 and $8,132,000, respectively. In addition, our training, maintenance and upgrade contracts backlog at February 23, 2007 and February 24, 2006, for work to be performed and revenue to be recognized after such dates under written agreements, was $1,276,000 and $1,774,000, respectively. Of the February 23, 2007 backlog, approximately 68% was concentrated between environmental and aircrew training systems and maintenance support, including $4,945,000 for a domestic automotive customer and $1,568,000 for Indonesia.

We expect to complete approximately 88% of the February 23, 2007 backlog prior to February 29, 2008, the end of our 2008 fiscal year. Of the February 24, 2006 backlog, we completed approximately 75% by February 23, 2007.

Competition

Our business strategy in recent years has been to seek niche markets in which there is limited competition. However, in some areas of our business we compete with well-established firms, some of which have substantially greater financial and personnel resources than we have.

Some competing firms have technical expertise and production capabilities in one or more of the areas involved in the design and production of physiological flight training equipment, environmental systems, and other specially designed products, and compete with us for this business. The competition for any particular project generally is determined by the technological requirements of the project, with consideration also being given to a bidder's reliability, product performance, past performance and price.

We face competition in the sale of the larger custom-designed industrial sterilizers both from other manufacturers and from our customers' in-house production capabilities.

We believe that we are a significant participant in the markets in which we compete, especially in the market for aircrew training systems where we believe that we are a principal provider of this type of equipment and training in our market area.

Compliance with Environmental Laws

We have not incurred during fiscal 2007, nor do we anticipate incurring during fiscal 2008, any material capital expenditures to maintain compliance with federal, state and local statutes, rules and regulations concerning the discharge of materials into the environment, nor do we anticipate that compliance with these provisions will have a material adverse effect on our earnings or competitive position.

Compliance with Export Controls

Depending on the product, customer, location and the application or use, many of our aeromedical products require an export license from the U.S. Commerce or State Department. We have implemented an Export License Compliance Program which covers all key aspects of the International Traffic in Arms (ITAR), as issued by the U.S. Department of Defense Trade Controls, an arm of the U.S. Department of State. Although most export licenses are readily obtainable in a reasonable timeframe, most of our international contracts for aeromedical equipment include the issuance of an export license as a "force majure" exception for any contract penalties or liquidated damages.

Employees

On February 23, 2007, we had 257 full-time employees, of which four were employed in executive positions, 64 were engineers, engineering designers, or draftspeople, 71 were administrative (sales, sales support, accounting, etc.) and clerical personnel, and 118 were engaged principally in production, operations and field support.

Item 1A. Risk Factors

RISKS PARTICULAR TO OUR BUSINESS

Our business is subject to numerous risks and uncertainties which could cause our actual operating results and developments to be materially different from those expressed or implied in any of our public announcements or filings including this Annual Report on Form 10-K for the year ended February 23, 2007. These risks and uncertainties include the following items. This list is not inclusive of all the risks and uncertainties associated with our business.

We have major litigation and claims in process and these require a significant amount of management time and effort. Additionally, legal costs are a major portion of our general and administrative spending, thus redirecting funds from other operating activities.

We are currently preparing our claim with the U.S. Government to go to trial in July of this year. Additionally, we anticipate that our litigation with Disney will be resolved this fiscal year. Legal and claims costs in fiscal 2007 were $1.4 million or 15% of total general and administrative spending and 8% of sales. It is expected that this spending level will increase in fiscal 2008 as litigation nears the trial stage. See Item 3 (Legal Proceedings) for further information on our litigation.

There is a risk of an unfavorable outcome in litigation and resulting potential negative financial impact on our operating results.

In one of our cases of commercial litigation currently in progress, we have been counter-sued for an amount in excess of $65 million. While we believe we have valid defenses to each of the counterclaims and intend to vigorously defend ourselves against these counterclaims, an unfavorable outcome could result in a material adverse effect on our financial position. With respect to our claim against the U.S. government, recoveries from prior claims of this nature have usually exceeded the carrying value of claims. However, this claim was filed in the Court of Federal Appeals whereas prior government claims were filed with the Armed Services Board of Contract Appeals (ASBCA), which has complicated the litigation process. This case is currently scheduled for trial in July 2007. Our claims require significant management time and effort. Also, there is no assurance that we will always have positive experience with regard to recoveries for our contract claims, whether at the carrying values of the claims or amounts in excess of the carrying values of the claims, and an unfavorable result could have a material adverse effect on our financial situation.

Our sources of revenues are not consistent; in any given fiscal year a substantial portion of our revenues is derived from a small number of customers that may not be recurring customers in future years.

In any given fiscal year, a substantial portion of our revenues is typically derived from a small number of customers. For example, in fiscal 2007 one customer Jupitor (Japan) represented approximately 19% of total sales. In fiscal 2006 we generated approximately 30% of our revenues from sales to two customers, L-3 Communications and the Pakistan Air Force. In fiscal 2005, we generated approximately 36% of our revenues from sales to four customers, the Royal Malaysian Air Force, the United Kingdom Ministry of Defense, the Army Corp of Engineers, and a domestic customer. Two customers accounted for 44% of our sales backlog at February 23, 2007. We cannot be certain that our most significant customers at any point in time will continue to order our products and services at the same level at which they have ordered them in the past. Due to the expensive nature and highly specialized market for our products and services, if any of these customers stops purchasing our products and services and we are unable to identify new customers in a timely manner, our business will be adversely affected.

If our funding source does not provide us with sufficient funds to operate our business, our results of operations and financial condition would be materially adversely affected.

Since 2003, H. F. Lenfest, a member of the Board of Directors of ETC, has provided significant funds which we have used to operate our business. Mr. Lenfest has also personally guaranteed our obligations to our commercial lender. In connection with our filing of this Annual Report on Form 10-K, Mr. Lenfest has entered into an agreement with ETC pursuant to which he has agreed, subject to the terms of the agreement, to continue to fund our operations through June 30, 2008, provided that ETC shall not request more than an additional $10 million in the aggregate from May 9, 2007, through June 30, 2008, including all requests made under our existing unsecured promissory note and equity credit line. We are also in discussions with a commercial lender to obtain debt financing for our operations, which Mr. Lenfest has agreed to personally guarantee if we enter into a financing arrangement with the lender. We can provide no assurance regarding our ability to secure commercial financing for our operations. If Mr. Lenfest is unable or unwilling to fund our operations and we were unable to identify a suitable funding source to replace the financing provided by Mr. Lenfest, our results of operations and financial condition would be materially adversely affected.

Our significant debt could adversely affect our financial resources and prevent us from satisfying our debt service obligations.

We have a significant amount of indebtedness. Our subordinated debt, $10,000,000 face value, carries an interest rate of 10%, although this rate has been temporarily reduced to 8% for the period from December 1, 2004 through November 30, 2007. Our outstanding preferred stock (issued in 2006 to Mr. Lenfest) carries a coupon of 6% per annum. On November 16, 2006, the Company executed an Unsecured Promissory Note (the “Lenfest Note”) in favor of Mr. Lenfest in the aggregate principal amount of $3,000,000. Pursuant to the terms of the Lenfest Note, ETC can borrow up to $3,000,000, in increments of $1,000,000, prior to the maturity date of

October 6, 2007. Any borrowings under the Lenfest Note will carry an interest rate of 6% per annum. To conserve cash outlay, Mr. Lenfest has agreed to defer the actual payment of all dividends on outstanding preferred stock until April 6, 2012 or upon 30 days written notice of demand, but not before June 30, 2008. Additionally, starting with the interest payment on our subordinated debt which was due on December 1, 2006, Mr. Lenfest has agreed to defer payment of interest until February 18, 2009 or until such time as we receive written demand notice of payment, but not before June 30, 2008. (Mr. Lenfest has also agreed to waive paying interest on deferred interest payments.) Since our bank agreement with PNC expires in June 2007 and both the Lenfest Equity Line and the Lenfest Note expire in October 2007, we will need to restructure or replace our financing arrangements. We may also incur additional indebtedness in the future. We may not generate sufficient cash flow from operations, or have future borrowings available to us, sufficient to pay our debt. During fiscal 2007 and 2006 we experienced negative cash flows from operations of $6,997,000 and $7,849,000, respectively. At May 11, 2007, our short-term debt was $2,000,000, total long-term debt was $10,000,000 and we had $6,000,000 of outstanding preferred stock. Our total stockholders' equity was $14,791,000. As of the date of this filing on Form 10-K, we had $9 million available under the Lenfest Equity Line and $1 million available under the Lenfest Note.

Our ability to make debt payments depends on future performance, which, to a certain extent, is subject to general economic, financial, competitive and other factors, some of which are beyond our control. We are currently in negotiations with a bank to establish a line of credit which will either replace or supplant our existing equity line and unsecured note with Mr. Lenfest. Based upon our current level of operations and anticipated growth, we believe that cash on hand and borrowings under either our existing arrangements or new arrangements with Mr. Lenfest and/or others will be adequate to meet our financial needs. There can be no assurance, however, that our business will generate sufficient cash flow from operations to enable us to pay our debts or to make necessary capital expenditures, that we will be successful in negotiating new financial arrangements, or that any refinancing of debt would be available on commercially reasonable terms.

Our substantial indebtedness could have important consequences including:

- our ability to obtain additional financing for working capital, capital expenditures, acquisitions or other purposes may be impaired or unavailable;
- a portion of cash flow may be required to pay interest expense, which will reduce the funds that would otherwise be available for operations and future business opportunities;
- a substantial decrease in net operating cash flows or an increase in expenses could make it difficult for us to meet our debt service requirements and force us to reduce or modify our operations;
- our significant debt may make us more leveraged than our competitors, which may place us at a competitive disadvantage;
- our significant debt may make us more vulnerable to a downturn in our business or in the economy generally;
- some of our existing debt contains financial and restrictive covenants that limit our ability to borrow additional funds, acquire and dispose of assets, and pay cash dividends;
- our subordinated debt bears a relatively high interest rate, reflecting the unsecured nature and correspondingly higher risk associated with this type of financing. This results in higher interest expense and potential use of cash; and
- although currently none of our debt bears interest at rates that vary with the prime rate of interest, it is expected that any additional debt which we might incur would carry a floating rate. If this were the case, any increases in the applicable prime rate of interest would reduce our earnings.

See the Liquidity and Capital Resources section of the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

We do not currently have a bank facility which can be used to borrow funds for operating purposes.

On November 16, 2006, we entered into a Letter Agreement with PNC Bank. This Letter Agreement amended, restated and replaced the existing PNC Credit Agreement. Pursuant to such agreement, PNC Bank (i) terminated our Credit Agreement dated as of February 18, 2003 (ii) re-approved our $5 million Line of Credit for Letters of Credit, and (iii) re-affirmed the Tangible Net Worth covenant (as defined in the Agreement) to a be a minimum of $9,000,000. The $5 million Line of Credit for Letters of Credit continued to be guaranteed by Mr. Lenfest. As of February 23, 2007, we had used approximately $2,607,000 of the availability under the PNC Agreement for international letters of credit.

We may need to obtain additional sources of capital in order to continue growing and operating our business. This capital may be difficult to obtain and the cost of this additional capital is likely to be relatively high.

Our subordinated debt agreement with Mr. Lenfest contains significant financial and operating covenants that limit the discretion of our management with respect to certain business matters. These covenants include, among others, restrictions on our ability to:

- declare or pay dividends or any other distributions to our securities holders;
- redeem or repurchase capital stock;
- incur certain additional debt;
- place liens on our assets;
- make certain payments and investments;
- sell or otherwise dispose of assets; and

- acquire or be acquired by other entities.

We must also meet certain financial ratios and tests under our subordinated agreement with Mr. Lenfest. If we do not comply with the obligations set forth in the agreement, it could result in an event of default, and possibly the acceleration of the related debt. Negative operating results would impact our future compliance with these covenants and could adversely affect our business.

We are currently in negotiations with a bank to establish a line of credit which will either replace or supplant our existing equity line and unsecured note with Mr. Lenfest. Because we have established businesses in many markets, significant fixed assets including a building, and other business assets which can be used for security, we believe that we will be able to locate such additional sources of capital, although there is no assuredness that we will be successful in this endeavor.

Effective May 9, 2007, the Company entered into a letter agreement with Mr. Lenfest ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

See the Liquidity and Capital Resources section of the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

We are attempting to introduce a new business model in two of our divisions.

In a major re-engineering of our aeromedical business, we are shifting our business model from reliance on building aeromedical products to providing both tactical combat flight training and G-force instruction. In fiscal 2006, we began construction of the National Aerospace Training and Research Center. This center, set to open in fiscal 2008, is an integrated pilot training center offering a complete range of aviation training and research support for military jet pilots and civil aviation as well as space travel and tourism.

In our ADMS division, we have contracted marketing studies to evaluate the best way to sell simulation training. The result was a decision to migrate to a services-based approach. We cannot be certain that we will be successful in this new approach of marketing training services.

We need to attain validation from the U.S. defense agencies of our Authentic Tactical Fighting Systems technology.

A second and equally challenging issue for our ATFS technology has been marketing this technology to the world's defense agencies. This is a new technology that goes contrary to conventional training belief that tactical flight and combat skills can only be learned in a flying aircraft. In January 2007 we achieved a major milestone in that the U.S. Air Force Research Lab prepared a business plan which incorporated the funds to build a joint strike fighter cockpit for the ATFS-400 simulator. This is the first step towards testing and validation of this technology by the U.S. military. At this point we cannot be certain that we will be able to overcome the conventional thinking on training nor achieve an acceptable level of validation with respect to the applicability and efficacy of ATFS training.

We have invested a significant amount of capital and resources in creating the NASTAR Center.

We cannot be certain that we will generate enough training revenues to recoup the major investment we have made to develop, produce and construct the equipment and building modifications for the NASTAR Center.

Our operations involve rapidly evolving products and technological change.

The rapid change of technology is a key feature of most of the industries in which our businesses operate. To succeed in the future, we will need to continue to design, develop, manufacture, assemble, test, market and support new products and enhancements on a timely and cost-effective basis. Historically, our technology has been developed through both customer-funded and internally funded research and development, and we expect this practice will continue to be required in the future. We cannot guarantee that we will continue to maintain comparable levels of research and development nor that this development will be customer-funded in the same ratio going forward. Reinvestment of operating funds and profits in an amount greater than currently earned may be required. Even so, we cannot be assured you that we will successfully identify new opportunities and continue to have the financial resources required to develop new products profitably. At the same time, products and technologies developed by others may render our products and systems obsolete or non-competitive.

Delays in the delivery of our products may prevent us from invoicing our costs and estimated earnings on uncompleted contracts.

In accordance with generally accepted accounting principles for long-term contracts, under the percentage of completion (“POC”) accounting method, we record an asset for our costs and estimated earnings that exceed the amount we are able to bill our customers on uncompleted contracts. At February 23, 2007, this asset totaled $2.8 million. Although a significant portion of these costs have been billed and collected since fiscal year-end, we cannot bill additional amounts unless and until we meet certain contractual milestones related to the production, delivery and integration of our products. Normally there will be a lag ranging from 6 to 24 months between performance and associated costs for these types of projects and billing and collection of payments. Our failure to meet these milestones by delivering and integrating our products in a timely manner may impact our ability to recover our costs and estimated earnings that exceeded our billings on uncompleted contracts, which could severely impact our cash flow.

In the event we suffer production delays, we may be required to pay certain customers substantial liquidated damages and other penalties.

The variety and complexity of our high technology product lines require us to deal with suppliers and subcontractors supplying highly specialized parts, operating highly sophisticated equipment and performing highly technical calculations. The processes of planning and managing production, inventory levels and delivery schedules are also highly complex and specialized. Many of our products must be custom designed and manufactured, which is not only complicated and expensive, but can also require long periods of time to accomplish. Slight errors in design, planning and managing production, inventory levels, delivery schedules, or manufacturing can result in unsatisfactory products that may not be correctable. If we are unable to meet our delivery schedules, we may be subject to penalties, including liquidated damages that are included in some of our customer contracts. Except for the RTAF contract (See Note 4 Accounts Receivable in the Notes to Consolidated Financial Statements section of the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K), our actual losses have been minimal, but we may incur substantial liquidated damages in the future in connection with product delays.

Our fixed-price and cost-reimbursable contracts may commit us to unfavorable terms.

Historically, we have provided our products and services primarily through fixed-price contracts. Fixed-price contracts provided approximately 92% of our sales for the fiscal year ended February 23, 2007. Under a fixed-price contract, we agree to perform the scope of work required by the contract for a predetermined contract price. Although a fixed-price contract generally permits us to retain profits if the total actual contract costs are less than the estimated contract costs, we bear the risk that increased or unexpected costs may reduce our profit or cause us to sustain losses on the contract. Therefore, unless there are customer-requested changes in scope or other changes in specifications which are reimbursable, we fully absorb cost overruns on fixed-price contracts and this reduces our profit margin on the contract. These cost overruns may result in us recognizing a loss on the contract. A further risk associated with fixed-price contracts is the difficulty of estimating sales and costs that are related to performance in accordance with contract specifications. Our failure to anticipate technical problems, estimate costs accurately or control costs during performance of a fixed-price contract may reduce our profitability or cause a loss.

Cost estimates used to account for contracts under the percentage of completion method may vary over time and impact future performance under these contracts.

We record sales and profits on a significant portion of our contracts using the POC method of accounting. On long-term contracts over $250,000 in value and over six months in length the POC revenue recognition method is utilized. Under this method a percentage is calculated based on costs incurred from inception to date on a contract as compared to the estimated total costs required to fulfill the contract. This percentage is then multiplied by the contract value to determine the amount of revenue to be recognized in any given accounting period. As a result, contract price and cost estimates on fixed-price contracts are reviewed periodically as the work progresses, and adjustments are reflected in income in the period when the estimates are revised. To the extent that these adjustments result in a loss, reduction or elimination of previously reported profits, we would recognize a charge against current earnings, which could be material and have a negative effect on our business, financial condition or results of operations. Although we believe that adequate provisions for losses for our fixed-prices contracts are recorded in our financial statements as required under accounting principles generally accepted in the United States of America, we cannot assure you that our contract loss provisions, which are based on estimates, will be adequate to cover all actual future losses.

Our contracts and subcontracts that are funded by the U.S. government or foreign governments are subject to government regulations, audits and other requirements.

Government contracts require compliance with various contract provisions and procurement regulations. The adoption of new or modified procurement regulations could have a material adverse effect on our business, financial condition or results of operations or increase the costs of competing for or performing government contracts. If we violate any of these regulations, then we may be subject to termination of these contracts, imposition of fines or exclusion from government contracting and government-approved subcontracting for some specific time period. In addition, our contract costs and revenues are subject to adjustment as a result of audits by government auditors. We reflect any adjustments required by government auditors in our financial statements. Although we have

thus far not been required to make any material audit adjustments, adjustments may be required in the future. In connection with our government contracts, we have been required to obtain bonds, letters of credit or similar credit enhancements. We cannot assure you that we will be successful in obtaining these types of credit enhancements or that the credit enhancements available will be affordable in the future.

Our contracts that are funded by the U.S. government or foreign governments are subject to a competitive bidding process that may affect our ability to win contract awards or renewals in the future.

Government contracts generally are awarded to us through a formal competitive bidding process in which we may have many competitors. Upon expiration, government contracts may be subject, once again, to the competitive bidding process. We cannot assure you that we will be successful in winning contract awards or renewals in the future. Our failure to renew or replace government contracts when they expire could have a material adverse effect on our business, financial condition or results of operations. Our contracts with domestic or foreign government agencies are subject to competition and are awarded on the basis of technical merit, personnel qualifications, experience and price. Our business, financial condition and results of operations could be materially adversely affected to the extent that government agencies believe our competitors offer a more attractive combination of the foregoing factors. In addition, new government contract awards also are subject to protest by competitors at the time of award that can result in the re-opening of the competition or evaluation process, the award of a contract to a competitor, or the re-opening of the competitive bidding process. We consider bid protests to be a customary element in the process of procuring government contracts. Other characteristics of the government contract market that may affect our operating results include the complexity of designs, the difficulty of forecasting costs and schedules when bidding on developmental and highly sophisticated technical work, and the speed with which product lines become obsolete due to technological advances and other factors characteristic of the market. Our earnings may vary materially on some contracts depending upon the types of government long-term contracts undertaken, the costs incurred in their performance, and the achievement of other performance objectives.

Our commercial contracts are subject to competition and strict performance and other requirements.

Although significant portions of our revenues are generated from the sale of our services and products in commercial markets, we cannot assure you that we will continue to compete successfully in these markets. Most of our commercial contracts contain fixed pricing which subjects us to substantial risks relating to unexpected cost increases and other factors outside of our control. We may fail to anticipate technical problems, estimate costs accurately, or control costs during performance of a fixed-price contract. Any of these failures may reduce our profit or cause a loss under our commercial contracts.

In connection with certain commercial contracts, we have been required to obtain bonds, letters of credit, or similar credit enhancements. We cannot assure you that we will be successful in obtaining these types of credit enhancements or that the credit enhancements available will be affordable in the future.

Under the terms of our commercial contracts, we typically must agree to meet strict performance obligations and project milestones, which we may not be able to satisfy. If we fail to meet these performance obligations and milestones, the other party may terminate the contract and, under certain circumstances, recover liquidated damages or other penalties from us which could have a negative effect on our business, financial condition or results of operations.

There are certain risks inherent in our international business activities, which constitute a significant portion of our business.

Our international business activities expose us to a variety of risks. Our international business including that from our foreign subsidiaries, accounted for approximately 62% of our sales in fiscal 2007 and 53% of our sales in fiscal 2006. We expect that international sales will continue to be a significant portion of our overall business in the foreseeable future. Our international business experiences many of the same risks our domestic business encounters as well as additional risks such as:

- the effects of terrorism;
- exchange rate fluctuations;
- a longer and more complicated collections cycle;
- a high degree of corruption in some countries;
- a general decline in the strength of the global economy;
- the effect of foreign military or political conflicts and turmoil;
- U.S. foreign policy decisions;
- the extent, if any, of anti-American sentiment;
- changes in foreign governmental trade, monetary and fiscal policies and laws;
- export controls; and
- political and economic instability.

The majority of our contracts which originate from ETC-Southampton are denominated in U.S. dollars. Except for intercompany work, and contracts with U.S. based companies, most of our contracts which originate from ETC-PZL are in Polish Zlotys.

Since most of our production and administrative costs are based in U.S. dollars, a weakening of the U.S. dollar currency versus other international currencies may make our pricing un-competitive when compared to foreign local in-country competitors.

Although we may be exposed to currency fluctuations, we are not engaged in any material hedging activities to offset this risk. With respect to currency risk, where we have a large on-going contract which is denominated in a foreign currency, we often establish local in-country bank accounts and fund in-country expenses in the local currency, thus creating a "natural" currency hedge for a portion of the contract.

Our international transactions frequently involve increased financial and legal risks arising from stringent contractual terms and conditions and widely differing legal systems, banking requirements, customs and standards in foreign countries. In addition, our international sales often include sales to various foreign government armed forces, with many of the same inherent risks associated with U.S. government sales discussed in this Annual Report on Form 10-K.

Legislative actions, higher director and officer insurance costs and potential new accounting pronouncements are likely to cause our general and administrative expenses to increase and impact our future financial condition and results of operations.

In order to comply with the Sarbanes-Oxley Act of 2002, as well as changes to the American Stock Exchange listing standards and rules adopted by the Securities and Exchange Commission ("SEC"), we have been required to strengthen our internal controls, hire additional personnel and retain additional outside legal, accounting and advisory services, all of which have caused and will continue to cause our general and administrative costs to increase. These and other costs of operating as a public company totaled approximately $600,000 in fiscal 2007. We anticipate that public company costs will continue to constitute a significant portion of our general and administrative spending going forward. Although we have not experienced any director and officer liability claims, these premiums are a significant part of our business insurance premiums and may increase as a result of the (i) high claims rates insurers have incurred with other companies over the past years (ii) the high stock ownership position of some of our non-affiliated shareholders, and (iii) our reduced operating performance. Changes in the accounting rules and auditing standards, including legislative and other proposals to account for employee stock options as a compensation expense, among others, could materially increase the expenses that we incur and report under generally accepted accounting principles and adversely affect our operating results.

Although up from the prior year, our fiscal 2008 opening backlog is still relatively lower than the balance at the beginning of most comparable prior fiscal periods. Additionally, our sales backlog is not necessarily indicative of revenues that we will actually realize in fiscal year 2008 or at all.

Our opening backlog for fiscal 2008 is approximately $14.8 million. The opening backlog for fiscal years 2002 through 2005 was in excess of approximately $20 million for each year. Although our open proposal quote log remains strong and we have recently experienced renewed customer interest in some significant international aeromedical proposals, there is no assurance that we will be able to bring a significant amount of these contracts to award status. Additionally, we may not actually generate revenues in fiscal 2008 for all items included in our backlog at the end of our 2007 fiscal year. While we estimate that approximately 88% of this $14.8 million backlog will be completed prior to the end of our 2008 fiscal year, we cannot be certain that these projects will be completed so that we can record these revenues by such date, or at all. During fiscal 2007, we recorded revenue on approximately 75% of our opening backlog. Our backlog includes the total value of all contracts less any revenue recorded on those contracts through the measurement date. Many of our government contracts are multi-year contracts and contracts with option years, and portions of these contracts are carried forward from one year to the next as part of our backlog. We cannot assure that cancellations or adjustments in the terms of these contracts might not occur.

Our operations could be hurt by terrorist attacks, war, disease and other activities or occurrences that make air travel difficult or reduce the willingness of our commercial airline customers to purchase our simulation products.

International sales accounted for 62% and 53% of our revenues for fiscal years 2007 and 2006, respectively. In the event terrorist attacks, war, disease or other activities or occurrences make air travel difficult or reduce the demand or willingness of our customers to purchase our commercial simulation products, our revenue may decline.

Geo-political and other factors may also limit or restrict our employees' ability to gain entrance to foreign locations to sell products or perform contract services.

There is limited trading activity in our common stock which could make it difficult for our investors to sell their shares of our common stock.

Our common stock is listed on the American Stock Exchange. Our average daily trading volume on the American Stock Exchange during fiscal 2007 was 3,690 shares; on the consolidated markets (which includes shares traded on the American Stock Exchange), the average daily volume was 5,645 shares. This limited trading activity may make it difficult for investors to sell larger blocks of our common stock at prevailing prices as there are generally a small number of participants in the market for our common stock and such sales may lower the market price of our common stock.

The market price of our common stock may be volatile.

The market price of securities of thinly traded public companies has historically faced significant volatility. Although our common stock is traded on the American Stock Exchange, it does not experience a significant average daily trading volume. Accordingly, if one stockholder elects to either purchase or sell a block of our common stock, it may have a significant effect on the price of our common stock. In addition, the stock market in recent years has experienced significant price and volume fluctuations that often have been unrelated or disproportionate to the operating performance of particular companies. Many factors that have influenced trading prices will vary from period to period, including:

- actual or anticipated operating results;
- changes in estimates by analysts;
- market conditions in the industry;
- announcements by competitors;
- results of litigation;
- regulatory actions; and
- general economic conditions.

Any of these events would likely affect the market price of our common stock.

Our quarterly operating results may vary significantly from quarter to quarter.

Our revenues and earnings may fluctuate from quarter to quarter based on factors that include the following:

- the number, size and scope of our projects;
- the mix of contracts (POC versus other);
- equipment purchases and other expenditures required for our business;
- the number of bid and proposal efforts undertaken;
- delays in sales or production;
- the level of employee productivity;
- the adequacy of our provisions for receivable, inventory and other losses;
- the accuracy of our estimate of resources required to complete ongoing projects; and
- general economic conditions.

Demand for our products and services in each of the markets we serve can vary significantly from quarter to quarter due to revisions in customer budgets or schedules and other factors beyond our control. Due to all of the foregoing factors, our results of operations may fall below the expectations of securities analysts and investors in a particular period. In this event, the price of our common stock may decline.

Our officers and directors own a significant amount of our common stock which permits them to exert significant influence over the direction of our business and affairs.

As of May 11, 2007, our directors and executive officers own an aggregate of approximately 45.2% on a fully converted basis of our outstanding common stock. Given our equity line agreement with H.F. Lenfest and the lack of a bank facility, it is expected that this percentage will increase if we request additional funds and issue additional preferred stock under this agreement. Accordingly, our directors and executive officers, if they act together, will be able to exert control over the direction of our business and affairs.

Item 2. Properties

We own our executive offices and principal production facilities located on a five acre site in the County Line Industrial Park, Southampton, Pennsylvania in an approximately 100,000 square foot steel and masonry building. Approximately 85,000 square feet of the building is devoted to manufacturing and 15,000 square feet of this building is devoted to office space. The original building was erected in 1969 and additions were most recently made in 2001. As of February 23, 2007, this property was pledged as collateral to secure the performance of our obligations under our subordinated debt financing with H.F. Lenfest. Additionally, we rent office space at various sales and support locations throughout the world and at ETC-PZL Aerospace Industries, our Polish subsidiary.

We consider our machinery and plant to be in satisfactory operating condition. Increases in the level of operations beyond what we expect in the current fiscal year might require us to obtain additional facilities and equipment.

Item 3. Legal Proceedings

In June 2003, Entertainment Technology Corporation (“EnTCo”), our wholly-owned subsidiary, filed suit against Walt Disney World Co. and other entities (“Disney”) in the United States District Court for the Eastern District of Pennsylvania, alleging breach of contract for, among other things, failure to pay all amounts due under a contract for the design and production of the amusement park ride “Mission: Space” located in Disney’s Epcot Center. In response, in August 2003, Disney filed counterclaims against both EnTCo and us (under a guarantee) for, among other things, alleged failures in performance and design in the contract. Disney is seeking

damages in excess of $65 million plus punitive damages. In December 2005, EnTCo filed a second suit against Disney, alleging breach of confidentiality and unfair trade practices. Both EnTCo and we believe that we have valid defenses to each of Disney's counterclaims and intend to vigorously defend ourselves against these counterclaims. Discovery is expected to be completed by June 2007 with pre-trial motions to follow. The case is not currently scheduled for trial. Neither EnTCo nor we are able to predict the outcome of this matter.

In May 2003 we filed a certified claim with the Department of the Navy seeking costs totaling in excess of $5.0 million in connection with a contract for a submarine rescue decompression chamber project. This claim against the Navy has followed the typical process of claim notification, preparation, submittal, government audit and review by the contracting officer. On July 22, 2004, the Navy's Contracting Officer issued a final decision denying the claim in full. In July 2005, we converted this claim into a complaint, which we filed in the Court of Federal Claims. This case is currently scheduled for trial in July 2007. While we intend to vigorously litigate this case, we cannot predict the outcome of this matter and an unfavorable result could have a material adverse effect on our financial position.

Certain other claims, suits, and complaints arising in the ordinary course of business have been filed or are pending against us. In our opinion, after consultation with legal counsel handling these specific maters, all such matters are reserved for or adequately covered by insurance or, if not so covered, are without merit or are of such kind, or involve such amounts, as would not have a significant effect on our financial position or results of operations if disposed of unfavorably.

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

No matters were presented to our stockholders during the fourth quarter of fiscal 2007.

PART II

Item 5. Market for the Registrant's Common Stock and Related Security Holder Matters

On April 7, 2006, ETC entered into a Preferred Stock Purchase Agreement (the "Lenfest Equity Agreement") with Mr. Lenfest. The Lenfest Equity Agreement, which ends on October 6, 2007, permitted us to unilaterally draw down up to $15 million in exchange for shares of our newly created Series B Cumulative Convertible Preferred Stock ("Preferred Stock"). The Preferred Stock provides for a dividend equal to six percent per annum. After three years, the Preferred Stock will be convertible, at Mr. Lenfest's request, into ETC common shares at a conversion price (the "Conversion Price") which will be set on the day of each draw down. The Conversion Price will be equal to the closing price of our common stock on the trading day immediately preceding the day in which the draw down occurs, subject to a floor price of $4.95 per common share. Drawdowns will not be permitted on any day when the Conversion Price would be less than this floor price. On the sixth anniversary of the Lenfest Equity Agreement, any issued and outstanding Preferred Stock will be mandatorily converted into ETC common stock at each set Conversion Price. The Lenfest Equity Agreement also allows us to redeem any outstanding Preferred Stock any time within its six-year term of the Lenfest Equity Agreement. Any issued and outstanding Preferred Stock will vote with the ETC common stock on an as converted basis.

In connection with the execution of the Agreement, in April 2006 we drew down $3 million by issuing 3,000 shares of Preferred Stock with a Conversion Price equal to $4.95 per share. Additionally, on July 31, 2006, we drew down an additional $3 million by issuing 3,000 shares of Preferred Stock at a conversion price equal to $6.68 per common share. In each instance, the proceeds were used for general corporate purposes.

Our common stock is traded on the American Stock Exchange under the symbol "ETC." As of May 11, 2007, the Company had 281 shareholders of record.

The following table sets forth the calendar quarter ranges of high and low sale prices for shares of the common stock for the periods indicated.

	Sale Prices	
	High	Low
Fiscal 2007		
First Quarter	$ 5.54	$ 4.60
Second Quarter	7.39	5.16
Third Quarter	6.39	4.71
Fourth Quarter	4.86	3.19
Fiscal 2006		
First Quarter	$ 6.05	$ 4.70
Second Quarter	5.85	4.85
Third Quarter	5.52	4.89
Fourth Quarter	5.22	4.75

On May 11, 2007, the closing price of our common stock was $3.80. We have never paid any cash dividends on our common stock and do not anticipate that any cash dividends will be declared or paid in the foreseeable future. Our current subordinated debt agreement with Mr. Lenfest prohibits the payment of any dividends without Mr. Lenfest's prior written consent.

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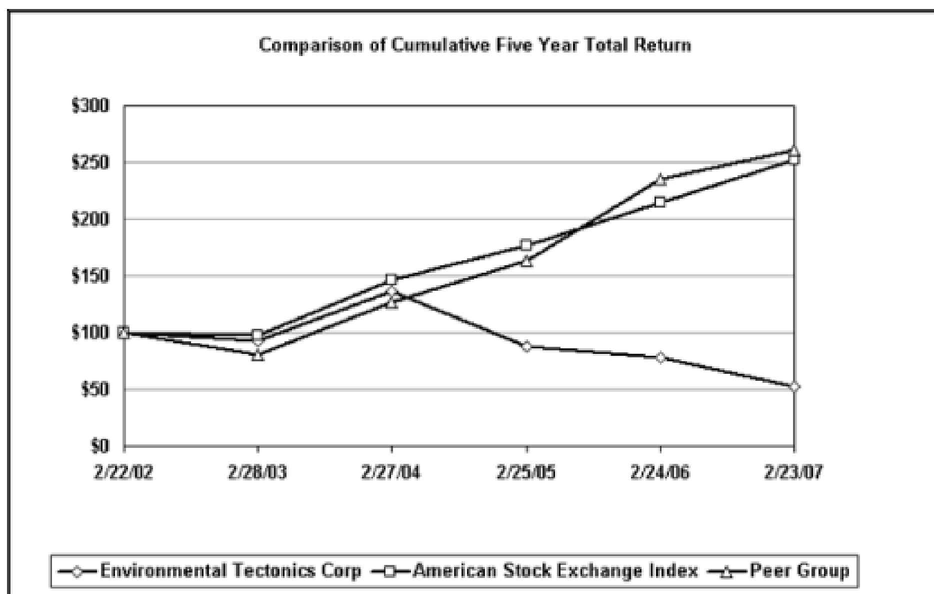
Total Return To Shareholders
(Includes reinvestment of dividends)

Company Name / Index	ANNUAL RETURN PERCENTAGE Years Ending 2/28/03	2/27/04	2/25/05	2/24/06	2/23/07
Environmental Tectonics Corp	-6.98	47.33	-35.52	-11.58	-33.53
American Stock Exchange Index	-3.00	51.02	20.89	21.37	17.65
Peer Group	-19.98	59.14	28.45	43.87	11.11

Company Name / Index	Base Period 2/22/02	INDEXED RETURNS Years Ending 2/28/03	2/27/04	2/25/05	2/24/06	2/23/07
Environmental Tectonics Corp	**100**	93.02	137.05	88.37	78.14	51.94
American Stock Exchange Index	**100**	97.00	146.49	177.09	214.94	252.88
Peer Group	**100**	80.02	127.34	163.58	235.33	261.48

Peer Group Companies

BVR SYSTEMS LTD
DATAKEY INC (Included through 2004. Acq'd by Safenet 1/2005)
EVANS & SUTHERLAND CMP CORP
RELM WIRELESS CORP
ROFIN SINAR TECHNOLOGIES INC
STANDARD MOTOR PRODS
UNITED INDUSTRIAL CORP



Item 6. Selected Consolidated Financial Data

See information appearing under the heading “Financial Review” in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

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

See information appearing under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to various market risks, including changes in interest rates. Market risk is the potential loss arising from adverse changes in market rates and prices, such as interest rates and foreign currency exchange rates. We do not enter into derivatives or other financial instruments for trading or speculative purposes. We also have not entered into financial instruments to manage and reduce the impact of changes in interest rates and foreign currency exchange rates although we may enter into such transactions in the future. Although currently none of our debt bears interest at rates that vary with the prime rate of interest, it is expected that any additional debt which we might incur would carry a floating rate. If this were the case, any increases in the applicable prime rate of interest would reduce our earnings. With respect to currency risk, where we have a contract which is denominated in a foreign currency, we often establish local in-country bank accounts and fund in-country expenses in the local currency, thus creating a “natural” currency hedge for a portion of the contract.

Item 8. Financial Statements and Supplementary Data

See the information appearing under the headings “Consolidated Financial Statements” and “Notes to Consolidated Financial Statements” in the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

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

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report, February 23, 2007 (the “Evaluation Date”), and, based on this evaluation, our chief executive officer and chief financial officer have concluded that these controls and procedures were effective as of the Evaluation Date.

Disclosure controls and procedures (as defined in Rules 13a-14(c) and 15(d)-14(c) under the Securities Exchange Act of 1934, as amended) are our internal controls and other procedures that are designed to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting. There was no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during our most recently completed fiscal quarter that has materially affected, or is reasonably to materially affect, our internal control over financial reporting.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of the inherent limitations of any internal control system, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.

PART III

Item 10. Directors and Executive Officers of the Registrant

The following table sets forth certain information, as of May 11, 2007, with respect to our directors and executive officers:

Name	Age	Served as Director or Officer Since (1)	Positions and Offices
William F. Mitchell (2)	65	1969	Chairman of the Board, President and Director
Howard W. Kelley (3)	65	2002	Director
George K. Anderson, M.D. (4)	61	2003	Director
H.F. Lenfest (5)	77	2003	Director
Alan M. Gemmill (6)	60	2006	Director
Duane D. Deaner (7)	59	1996	Chief Financial Officer

(1) Directors are elected for one-year terms.

(2) Mr. Mitchell has been our Chairman of the Board, President and Chief Executive Officer since 1969, except for the period from January 24, 1986 through January 24, 1987, when he was engaged principally in soliciting sales for our products in the overseas markets. Mr. Mitchell received a Bachelor of Science degree in physics from Drexel University and has completed graduate work in mechanical and electrical engineering. He is a member of the ASME and Drexel University engineering advisory boards. Additionally, he is a member of the Society of Automotive/Aerospace Engineering, the International Society of Pharmaceutical Engineering, the Undersea and Hyperbaric Medical Society, the Aerospace Medical Association, the American Society of Mechanical Engineering and the Institute of Environmental Sciences.

(3) Mr. Kelley is President of Sally Corporation, Jacksonville, Florida, which is one of the oldest and largest designers and fabricators of animation robotics and dark ride attractions used worldwide in theme parks, museums and entertainment attractions. Mr. Kelley is also Chairman of the Board of American Access Technologies, Inc. (NASDAQ:AATK). AATK is a Florida-based manufacturer of zone cabling and wireless equipment. He previously spent over 25 years in the broadcasting industry, including ten years in television management as a news director and later as Vice President and General Manager of Channel 12 WTLV (NBC) in Jacksonville, Florida. He is the former Chairman of the Board of Tempus Software, a medical software development firm located in Jacksonville, Florida. He has also previously served as broadcast strategic planner for a major U.S. communications company and as director of several U.S. technology firms with international business activities. In the academic arena, Mr. Kelley serves as an executive professor at the University of North Florida College of Business Administration, and is a college adjunct instructor on Internet technology and E-commerce on the Internet. He is a graduate of the University of Florida and Harvard Business School PMD.

(4) Dr. Anderson is an experienced physician executive. He served in the Air Force as a flight surgeon, aerospace medicine staff officer, and commander of several medical organizations in Korea, Germany, and United States. He retired from active duty in the grade of Major General. Following his thirty years of military service, he transitioned to executive positions in the private sector. He served as Chief Executive Officer of the Koop Foundation from 1997 to 1998 and as Chief Executive Officer at Oceania, Inc., a medical software company, from 1999 to 2001. A period of practice as an independent medical technology consultant was followed by his current role as Executive Director of the Association of Military Surgeons of the United States (AMSUS). AMSUS, the nonprofit Society of the Federal Health agencies, operates from a headquarters located in Bethesda, Maryland.

(5) Mr. Lenfest practiced law with Davis Polk & Wardwell before joining Triangle Publications, Inc., in Philadelphia as Associate Counsel in 1965. In 1970, Mr. Lenfest was placed in charge of Triangle's Communications Division, serving as Editorial Director and Publisher of Seventeen Magazine and President of the CATV Operations. In 1974, Mr. Lenfest, with the support of two investors, formed Lenfest Communications, Inc., which purchased Suburban Cable TV Company and Lebanon Valley Cable TV Company from Triangle with a total of 7,600 subscribers. In January 2000, Mr. Lenfest sold his cable television operations, which by then served 1.2 million subscribers, to Comcast Corporation. Mr. Lenfest is the owner of various other businesses and is active in many philanthropic activities including as Chairman of the Board of the Philadelphia Museum of Art, the Curtis Institute, and the Lenfest Foundation. Mr. Lenfest is a graduate of Washington and Lee University and Columbia Law School.

(6) Mr. Gemmill is a retired U.S. Navy Rear Admiral. He graduated from the University of Arizona with a B.S. in Aerospace Engineering and was commissioned through Aviation Officer Candidate School. He began his career flying F-4 Phantoms before graduating first in his class from U.S. Naval Test Pilot School in Patuxent River, Maryland in 1974. After a brief stint as a test pilot and instructor, Mr. Gemmill then served numerous positions in Fighter Squadrons and on various ships including two deployments to the Arabian Gulf during Desert Shield and Desert Storm. From 1995 through 1999 he served as Deputy for Readiness and Deputy for Operations for the U.S. Pacific Command and as Assistant Deputy Chief of Staff for Aviation, U.S. Marine Corps. He was promoted to Rear Admiral on October 30, 1997. His last assignment before retirement from the Navy was as Head, Aircraft Carriers Program and Head, Naval Aviation Training. Rear Admiral Gemmill has almost 4,000 flight hours and 1,000 carrier landings. He has a Master of Science in Systems Management from the University of Southern California. His personal decorations include the Defense Superior Service Medal, Legion of Merit, Meritorious Service Medal, the Strike/Flight Air Medal and the Navy Commendation Medal. He is currently Director Defense Business Services for Bearing Point of McLean, VA.

(7) Mr. Deaner has served as our Chief Financial Officer since January 1996. Mr. Deaner served as Vice President of Finance for Pennfield Precision Incorporated from September 1988 to December 1995. Mr. Deaner received an MBA in Finance from Temple University and a B.A. in Mathematics from Millersville University in Pennsylvania.

Committees of the Board of Directors

During the fiscal year ended February 23, 2007, the Board of Directors held four meetings. All members of the Board of Directors attended all of the Board meetings held while they were members, except for Mr. Lenfest, who did not attend two meetings.

We have three Board Committees: Audit, Compensation and Governance and Nominating. The members of each committee are identified in the following table and each committee and its function is described below.

Name of Director	Independent	Audit	Compensation	Governance and Nominating
Howard W. Kelley	Yes	Chair	X	X
Dr. George K. Anderson	Yes	X	X	Chair
Alan Mark Gemmill	Yes	X	Chair	X
Number of Meetings Held in Fiscal Year		7	3	3

During the fiscal year ended February 23, 2007, we had an Audit Committee consisting of Messrs. Kelley, Gemmill and Anderson. Mr. Kelley serves as the Chairman and the “financial expert” (as defined by the American Stock Exchange) and has been designated as the Audit Committee Financial Expert as defined by the rules of the Securities and Exchange Commission. In addition, all members of the Audit Committee meet the financial literacy requirements of the American Stock Exchange and are independent under the rules of the American Stock Exchange. Among other responsibilities, the Audit Committee meets (via face-to face or via telephone) with the external auditors to review and make recommendations to management concerning (if appropriate) the quarterly and annual financial results and the reports on Forms 10-Q and 10-K. The Audit Committee held three general face-to-face meetings and four telephonic meetings (to review the financial results with our external auditors) during the year ended February 23, 2007. The Audit Committee is directly responsible for the appointment, compensation, retention and oversight of our independent accountants in their preparation or issuance of an audit report or the performance of other audit and review services.

Messrs. Kelley, Gemmill and Anderson also served on our Compensation Committee during the year ended February 23, 2007, with Mr. Gemmill serving as Chairman. The Compensation Committee is charged with reviewing the compensation and incentive plans of officers and key personnel. This Committee met three times during the fiscal 2007 year.

Messrs. Kelley, Gemmill and Anderson also served on our Nominating and Governance Committee during the year ended February 23, 2007, with Dr. Anderson serving as Chairman. The Nominating and Governance Committee is charged with finding and recommending new Board members and with ensuring our compliance with all regulatory governance requirements. This Committee met three times during the 2007 fiscal year.

Code of Ethics

We have adopted a Code of Ethics, which applies to our chief executive officer, chief financial officer, controller and other senior financial officers. We have also adopted a Company Code of Conduct that applies to our directors, officers and all employees. The Code of Ethics and the Company Code of Conduct were each approved and adopted by our Board of Directors in April 2004. The

Code of Ethics and the Company Code of Conduct are posted on our website, which is located at *www.etcusa.com.* We will also disclose any amendments or waivers to the Code of Ethics or the Company Code of Conduct on our website.

In addition, we have adopted a Whistleblower Policy and an Insider Trading Policy, both of which are posted on our website.

Compliance With Section 16(a) of the Exchange Act

Section 16(a) of the Securities Exchange Act of 1934 requires our officers and directors, and persons who own more than ten percent of a registered class of our equity securities to file reports of ownership and changes in ownership with the Securities and Exchange Commission and the American Stock Exchange. Officers, directors and greater than ten percent shareholders are required by SEC regulations to furnish us with copies of all Section 16(a) reports they file. The rules of the SEC regarding the filing of Section 16(a) reports require that "late filings" of Section 16(a) reports be disclosed in our proxy statement.

Based solely on our review of the copies of such forms which we received, or written representations from reporting persons that no Section 16(a) reports were required for those persons, Mr. Kelley had two late filings and Mr. Lenfest had one late filing. We believe that our greater than ten percent beneficial owners complied with all applicable filing requirements.

Item 11. Executive Compensation

COMPENSATION DISCUSSION AND ANALYSIS

Objectives and Philosophy of Executive Compensation

ETC's executive compensation program is administered by the Compensation Committee of the Board of Directors. The Compensation Committee is composed of Alan M. Gemmill who serves as Chairman, George K. Anderson, M.D., MPH, and Howard W. Kelley, each of whom is independent under the relevant rules of the Securities and Exchange Commission and American Stock Exchange. The Compensation Committee is responsible for developing and implementing an executive compensation program that takes into account ETC's business strategy, the need for highly qualified management and other relevant factors. The executive compensation program is structured to link executive compensation to the overall performance of ETC and to use ETC's stock as a compensation medium designed to more closely align the interests of the executive management team with the interests of ETC's shareholders.

The Compensation Committee's philosophy in establishing its compensation policies is to maximize the possibilities for enhancing shareholder value by closely aligning compensation for ETC's executive officers with the profitability of ETC. In this regard, it is considered essential to the success of ETC that its compensation policies enable ETC to attract, retain and satisfactorily reward executive officers who are contributing to the long-term growth and success of ETC. William F. Mitchell, President and Chief Executive Officer, and Duane D. Deaner, Chief Financial Officer, are ETC's Named Executive Officers under applicable Securities and Exchange Commission regulations.

Primary Components of Executive Compensation

In 2004, the Board of Directors adopted and approved a Compensation Committee Charter which sets forth the principles and policies followed by the Compensation Committee in connection with executive compensation. A copy of ETC's Compensation Charter is available on ETC's corporate website (http:www.etcusa.com).

The primary components of ETC's executive compensation program consist of base salary, annual cash bonus incentive opportunities and long-term incentive opportunities in the form of options to acquire common stock.

Base Salary

Base salary levels for ETC's executive officers are set near the average base salary levels paid by other companies within ETC's peer group. William F. Mitchell, President and Chief Executive Officer, received a base salary of $225,000 in the 2007 fiscal year. Duane D. Deaner, Chief Financial Officer, received a base salary of $98,000 in the 2007 fiscal year. The Compensation Committee has responsibility for setting Mr. Mitchell's base salary and approved Mr. Mitchell's employment agreement at the time it was entered into. Mr. Mitchell has responsibility for setting the base salary of the other officers and employees, including the base salary of Mr. Deaner.

Short-term Incentive Compensation

Based on the Compensation Committee's review of ETC's performance for the fiscal year ended February 23, 2007, and the performance of its management team, no cash incentive compensation awards were made to any officers or key employees.

The Compensation Committee's review included an assessment of ETC's performance against financial and non-financial targets, set at the beginning of the 2007 fiscal year (in February 2006), relating to bookings, sales, net income, stock price and individually tailored goals. The targets reflected the Board of Directors' determination of the appropriate goals for ETC.

Under the Chief Executive Officer Bonus Plan (the "CEO Plan"), Mr. Mitchell was eligible to receive a bonus for fiscal 2007 (i) in an amount up to 25% of base salary if ETC attained predetermined goals regarding sales and net income and (ii) in an amount from 25% to 100% of base salary if ETC's stock price performance met predetermined goals. Based on these criteria, Mr. Mitchell did not receive any bonus for fiscal 2007. Under the Executive Management/Key Employee Plan (the "Executive Management Plan") officers (other than CEO) are eligible to receive bonuses in an amount up to 25% of base salary if the predetermined goals are attained.

Under the CEO Plan and Executive Management Plan, 75% of any bonuses awarded for a particular fiscal year is paid in May of the following fiscal year, and the remaining 25% is paid in equal installments over the succeeding five years with interest at the average prime rate being charged over the period by ETC's principal bank. Deferred bonus amounts are not vested until paid and are subject to continued employment. No bonus awards were earned or paid for the fiscal year ended February 23, 2007, as ETC did not achieve the predetermined goals.

Beginning during the fiscal year ended February 23, 2007, certain key employees, including Mr. Deaner, were given the opportunity to earn additional compensation of up to approximately 10% of their base salary by completing specific annual objectives tailored to their individual areas of responsibility. Under this program, in fiscal 2007 a total of $30,000 was paid to four key employees, including $6,000 paid to Mr. Deaner. This program must be re-authorized on an annual basis and is subject to cancellation at any time.

Long-Term Incentive Compensation

ETC's 1998 Incentive Stock Option Plan is a long-term plan designed not only to provide incentives to management, but also to align a significant portion of the executive compensation program with shareholder interests. The 1998 Incentive Stock Option Plan permits ETC to grant certain officers and employees a right to purchase shares of stock at the fair market value per share at the date the option is granted. A total of 44,639 options were granted to executive officers and employees in fiscal 2007. In granting stock options to officers and employees, the Compensation Committee takes into account ETC's financial performance, its long-term strategic goal of increasing shareholder value, the employee's level of responsibility and his continuing contributions to ETC. The amount of the award to any employee is based on the employee's base salary and the total award for any employee is limited to one percent (1%) of total outstanding shares on award date. Under the program, during fiscal 2007, Mr. Deaner was awarded options to purchase 642 shares of ETC's common stock. Mr. Mitchell has never received any options to purchase shares of ETC's common stock under this program.

Option Grant Date Pricing

The Compensation Committee administers ETC's 1998 Incentive Stock Option Plan. Mr. Mitchell makes recommendations with respect to option grants but all other determinations to award options to purchase ETC's common stock are made by the Compensation Committee and in all instances the exercise price is equal to ETC's stock price on the date the Compensation Committee approves such option grants.

Given the relatively low amount of option grants made by ETC (options to purchase a total of 44,639 shares of ETC's common stock were awarded in fiscal 2007 and options to purchase only 642 shares of ETC's common stock were awarded to a Named Executive Officer in fiscal 2007), the Compensation Committee does not actively attempt to coordinate option grants based on the presence or absence of material non-public information.

Chief Executive Officer Employment Agreement

On July 24, 2006, ETC entered into an employment agreement with William F. Mitchell pursuant to which Mr. Mitchell continues to be employed as the President and Chief Executive Officer. Mr. Mitchell has been the Chairman of the Board, President and Chief Executive Officer of ETC since 1969, except for the period from January 24, 1986 to January 24, 1987 during which he was engaged principally in soliciting sales for ETC's products in the overseas market.

Under the employment agreement, Mr. Mitchell is entitled to receive a base salary of $225,000, which is subject to increase annually based on a review of Mr. Mitchell's performance by ETC's Board of Directors. Mr. Mitchell is also entitled to receive a bonus based on a formula and targets set forth in the CEO Plan.

The term of the employment agreement is three years, and, if ETC does not renew the employment agreement for additional three-year periods, Mr. Mitchell is entitled to terminate the employment agreement and receive certain benefits under the terms of the employment agreement including, without limitation, three years of base salary, bonuses and participation in various benefit plans. The employment agreement also provides Mr. Mitchell with three years of base salary, bonuses, and participation in various benefit plans of ETC if his employment is terminated due to a disability, by ETC without cause, or if Mr. Mitchell terminates his employment with ETC for good reason, including a change in control of ETC, each as defined in the employment agreement.

Chief Financial Officer Employment Agreement

On November 1, 2005, ETC entered into an employment agreement with Duane D. Deaner pursuant to which Mr. Deaner continues to be employed as the Chief Financial Officer. Mr. Deaner has been the Chief Financial Officer of ETC since 1996.

Under the employment agreement, Mr. Deaner is entitled to receive a base salary of $98,000, which is subject to increase annually based on a review of his performance. Mr. Deaner is also entitled to receive a bonus under the Executive Management Plan.

The term of the employment agreement is two years, and, if ETC does not renew the employment agreement for additional two-year periods, Mr. Deaner is entitled to terminate the employment agreement and receive certain benefits under the terms of the employment

agreement including, without limitation, two years of base salary, bonuses and participation in various benefit plans. The employment agreement also provides Mr. Deaner with two years of base salary, bonuses, and participation in various benefit plans of ETC if his employment is terminated due to a disability, by ETC without cause, or if Mr. Deaner terminates his employment with ETC for good reason, including a change in control of ETC, each as defined in his employment agreement.

REPORT OF THE COMPENSATION COMMITTEE

The information contained in this Compensation Committee Report shall not be deemed to be "filed" or incorporated by reference in future filings with the Securities and Exchange Commission, except to the extent ETC specifically incorporates it by reference into a document filed under the Securities Act of 1933 or the Securities Exchange Act of 1934.

The Compensation Committee of the Board of Directors has reviewed and discussed the Compensation Discussion and Analysis with management and, based on that review and discussion, the Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this report.

Submitted by the Compensation Committee of the Board of Directors,
Alan M. Gemmill, Chairman
George K. Anderson, M.D., MPH
Howard W. Kelley

FISCAL 2007 SUMMARY COMPENSATION TABLE

The following Summary Compensation Table sets forth the compensation of our Named Executive Officers for the fiscal year ended February 23, 2007.

Name and Principal Position (a)	Year (b)	Salary (c)	Bonus (d)	Stock Awards (e)	Option Awards (f)	Non-Equity Incentive Plan Compensation (g)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (h)	All Other Compensation (i)	Total (j)
William F. Mitchell[1] Chairman of the Board, Chief Executive Officer, President and Director	2007	$225,000	—	—	—	—	—	$ 72,000[2]	$297,000
Duane D. Deaner [3] Chief Financial Officer	2007	$ 98,000	$6,000	—	—	—	—	$ 3,000[4]	$ 107,000

The elements of the Summary Compensation Table are discussed in the Compensation Discussion and Analysis above.

1 ETC is party to an employment agreement with Mr. Mitchell, pursuant to which Mr. Mitchell serves as President and Chief Executive Officer. The terms and conditions of Mr. Mitchell's employment agreement is summarized above under "Primary Components of Executive Compensation-Chief Executive Officer Employment Agreement."

2 Consists of $60,000 paid to Mr. Mitchell in connection with ETC's use of Mr. Mitchell's properties, $6,000 in automobile allowance payments for Mr. Mitchell's company automobile and $6,000 in life insurance premium payments.

3 ETC is a party to an employment agreement with Mr. Deaner, pursuant to which Mr. Deaner serves as Chief Financial Officer. The terms and conditions of Mr. Deaner's employment agreement is summarized above under "Primary Components of Executive Compensation-Chief Financial Officer Employment Agreement."

4 Consists of ETC's contribution on behalf of Mr. Deaner pursuant to ETC's Retirement Savings Plan.

FISCAL 2007 GRANTS OF PLAN-BASED AWARDS

The following Grants of Plan-Based Award Table sets forth the options to purchase shares of ETC common stock awarded to our Named Executive Officers for the fiscal year ended February 23, 2007.

Name	Grant Date	Estimated Future Payouts Under Equity Incentive Plan Awards Threshold (#)	Target (#)	Maximum (#)	Exercise or Base Price of Option Awards ($/Sh)	Grant Date Fair Value of Option Awards
William F. Mitchell Chairman of the Board, Chief Executive Officer, President and Director	—	—	—	—	—	
Duane D. Deaner Chief Financial Officer	9/21/06	—	642	—	$ 6.07	$ 3,897

The elements of the Grants of Plan-Based Awards Table are discussed in the Compensation Discussion and Analysis above.

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

This table summarizes the equity awards held by our Named Executive Officers as of February 23, 2007.

Name (a)	Number of Securities Underlying Unexercised Options (#) Exercisable (b)	Number of Securities Underlying Unexercised Options (#) Unexercisable (c)	Option Exercise Price ($) (e)	Option Expiration Date (f)
William F. Mitchell Chairman of the Board, Chief Executive Officer, President and Director	—	—	—	—
Duane D. Deaner	10,000	—	$ 7.81	2/25/09
Chief Financial Officer	2,881	—	$ 7.375	1/03/11
	3,489	3,489	$ 7.24	9/15/14
	—	642	$ 6.07	9/21/16

FISCAL 2007 OPTION EXERCISES AND STOCK VESTED TABLE

During Fiscal 2007, neither of the Named Executive Officers exercised any options.

Potential Payments Upon Termination or Change-In-Control

As discussed in the Compensation Discussion and Analysis above, we entered into an employment contract with Mr. Mitchell, our Chief Executive Officer, on July 24, 2006, which provides Mr. Mitchell with three years of base salary, bonuses and participation in various benefit plans of ETC if his employment is terminated due to a disability, by ETC without cause, or if Mr. Mitchell terminates his employment with ETC for good reason, including a change in control of ETC, each as defined in his employment agreement.

Also, as discussed in the Compensation Discussion and Analysis above, we entered into an employment contract with Mr. Deaner, our Chief Financial Officer, on November 1, 2005, which provides Mr. Deaner with two years of base salary, bonuses and participation in various benefit plans of ETC if his employment is terminated due to a disability, by ETC without cause, or if Mr. Deaner terminates his employment with ETC for good reason, including a change in control of ETC, each as defined in his employment agreement.

Compensation of Directors

During fiscal 2007, our directors who did not serve as officers were paid a fee of $2,000 (either in cash or equivalent value of common stock of the Company) per quarter for attending Board of Directors and committee meetings. Additionally, under a plan approved by our shareholders at the 2005 Annual Meeting of Shareholders, non-employee directors may be awarded options to purchase common stock of the Company at fair market value . Pursuant to this plan, in February 2006, awards to purchase common stock were given as follows: Dr. Anderson, 50,000 options; Mr. Kelley, 25,000 options and Mr. Gemmill, 5,000 options.

FISCAL 2007 DIRECTOR COMPENSATION TABLE

Name (a)	Fees Earned or Paid in Cash ($) (b)	Stock Awards ($)[5] (c)	Option Awards ($) (d)	Non-Equity Incentive Plan Compensation ($) (e)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($) (f)	All Other Compensation ($) (g)	Total ($) (h)
William F. Mitchell [5]	—	—	—	—	—	—	—
George K. Anderson, M.D. [6]	$8,000	—	—	—	—	—	$8,000
Alan M. Gemmill[7]	$8,000	—	—	—	—	—	$8,000
Howard W. Kelley[8]	—	$8,000	—	—	—	—	$8,000
H. F. Lenfest[9]	$2,000	$4,000	—	—	—	—	$6,000

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5 ETC used the closing price of its common stock on the date of grant as reported on the American Stock Exchange to compute the value of these awards.

6 Mr. Mitchell did not hold any options to purchase shares of our common stock as of February 23, 2007.

7 Dr. Anderson held options to purchase an aggregate of 50,000 shares of our common stock as of February 23, 2007

8 Mr. Gemmill held options to purchase an aggregate of 5,000 shares of our common stock as of February 23, 2007.

9 Mr. Kelley held options to purchase an aggregate of 25,000 shares of our common stock as of February 23, 2007.

10 Mr. Lenfest did not hold any options to purchase shares of our common stock as of February 23, 2007.

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

The following table sets forth, as of May 11, 2007, the number of shares and percentage of our common stock owned beneficially by each director, each executive officer named in the Summary Compensation Table, and each person holding, to our knowledge, more than 5% of our outstanding common stock. The table also sets forth the holdings of all directors and executive officers as a group.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership (1)	Percent of Common Stock
William F. Mitchell (2) c/o Environmental Tectonics Corporation County Line Industrial Park Southampton, PA 18966	1,066,398(3)	11.8%
Howard W. Kelley (4) c/o Sally Corporation 745 West Forsyth Street Jacksonville, FL 32204	30,807(5)	*
George K. Anderson, M.D. (4) 8 Little Harbor Way Annapolis, MD 21403	51,100(6)	1.0%
H.F. Lenfest (4) c/o The Lenfest Group Fire Tower Bridge-Suite 460 300 Barr Harbor Drive West Conshohocken, PA 19428	4,250,931(7)	35.7%
Alan M. Gemmill (4) 941 Upper Hastings Way Virginia Beach, VA 23452	5,200(8)	*
T. Todd Martin, III 50 Midtown Park East Mobile, AL 36606	1,989,592(9)	22.0%
Emerald Advisors, Inc. 1703 Oregon Pike Suite 101 Lancaster, PA 17601	725,998(10)	8.0%
Pete L. Stephens, M.D. 31 Ribaut Drive Hilton Head Island, SC 29926	653,723(11)	7.2%
All directors and executive officers as a group (6 persons)	5,420,806(12)	45.2%

* less than 1%

(1) Beneficial ownership has been determined in accordance with Rule 13d-3 under the Securities Exchange Act of 1934. Unless otherwise noted, we believe that all persons named in the table have sole voting and investment power with respect to all shares of our common stock beneficially owned by them.

(2) Chairman of the Board, President, Chief Executive Officer and Director of the Corporation.

(3) Includes 45,200 shares of common stock held by Mr. Mitchell's wife.

(4) Director of the Company.

(5) Includes 25,000 shares of common stock which may be acquired upon the exercise of options granted under our Non-Employee Director Stock Option Plan that are presently exercisable.

(6) Includes 50,000 shares of common stock which may be acquired upon the exercise of options granted under our Non-Employee Director Stock Option Plan that are presently exercisable.

(7) Includes 1,818,181 shares of common stock issuable upon conversion of a promissory note in the principal amount of $10,000,000, 606,060 shares of common stock issuable upon conversion of 3,000 shares of Preferred Stock issued on April 6, 2006, and 449,101 shares of common stock issuable upon conversion of Preferred Stock issued on July 31, 2006.

(8) Includes 5,000 shares of common stock which may be acquired upon the exercise of options granted under our Non-Employee Director Stock Option Plan that are presently exercisable.

(9) Includes 1,928,692 shares of common stock owned by Advanced Technology Asset Management, LLC (formerly ETC Asset Management, LLC) (“ATAM”), a limited liability company of which T. Todd Martin, III is manager. Also includes 26,900 shares owned by Allied Williams Co, Inc., a corporation of which Mr. Martin is an officer and director, 17,000 shares owned by Equity Management, LLC, a limited liability company of which Mr. Martin is manager, 7,000 shares owned by trusts of which Mr. Martin is trustee, and 10,000 shares owned by Perdido Investors, LLC, of which Mr. Martin is the manager.

(10) Emerald Advisors, Inc., has sole voting power with respect to 293,048 shares of common stock and sole dispositive power over 725,998 shares of common stock.

(11) Includes 638,023 shares of common stock held jointly with Dr. Stephens’ wife and 15,700 shares of common stock held by Dr. Stephens’ children.

(12) Includes 80,000 shares of common stock which may be acquired by Members of the Board upon the exercise of options granted under our Non-Employee Director Stock Option Plan that are presently exercisable, 1,818,181 shares of common stock issuable upon conversion of a promissory note in the principal amount of $10,000,000, 606,060 shares of common stock issuable upon conversion of 3,000 shares of Preferred Stock issued on April 6, 2006, and 449,101 shares of common stock issuable upon conversion 3,000 shares of Preferred Stock issued on July 31, 2006, all of which may be acquired by Mr. Lenfest, and 16,370 shares of common stock which may be acquired by Duane Deaner, our chief financial officer, upon the exercise of options granted under our Incentive Stock Option Plan that are presently exercisable.

For information regarding our equity compensation plans, please see the Equity Compensation Plan Information section of the Annual Report to Stockholders attached hereto as Exhibit 13 and incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions and Director Independence

Related Transactions. On February 19, 2003, we completed a refinancing of our indebtedness with the PNC Bank, National Association and H.F. Lenfest in the aggregate amount of $29,800,000. Pursuant to the terms of a Convertible Note and Warrant Purchase Agreement, dated February 18, 2003, between us and Mr. Lenfest, we issued to Mr. Lenfest (i) a 10% senior subordinated convertible promissory note in the original principal amount of $10,000,000 and (ii) warrants to purchase 803,048 shares of our common stock. As a condition to closing the financing, we appointed Mr. Lenfest to our Board of Directors. On October 25, 2004, Mr. Lenfest executed a Limited Guaranty Agreement which guaranteed our $5 million Letter of Credit facility with PNC, and in connection therewith, we issued a Stock Purchase Warrant to Mr. Lenfest pursuant to which Mr. Lenfest was entitled to purchase up to 200,000 shares of our common stock at an exercise price equal to the lesser of $4.00 per share or 2/3 of the average daily high and low closing price of our common stock during the 25 day trading period immediately preceding the date of exercise. On February 14, 2005 Mr. Lenfest exercised all of his outstanding warrants and received 1,003,048 shares of unregistered common stock and purchased an additional 373,831 shares of unregistered common stock for approximately $2 million. Under the American Stock Exchange listing rules, shareholder approval was required for this transaction so it was included as a proxy item at our annual meeting in 2005. Shareholder approval was received at our 2005 annual meeting.

On April 6, 2006, we entered into a Preferred Stock Purchase Agreement (the “Lenfest Equity Agreement”) with Mr. Lenfest. The Agreement, which ends on October 6, 2007, permitted us to unilaterally draw down up to $15 million in exchange for shares of our newly created Series B Cumulative Convertible Preferred Stock (“Preferred Stock”). The Preferred Stock provides for a dividend equal to six percent per annum. After three years, the Preferred Stock will be convertible, at Mr. Lenfest’s request, into ETC common shares at a conversion price (the “Conversion Price”) which will be set on the day of each draw down. The Conversion Price will be equal to the closing price of our common stock on the trading day immediately preceding the day in which the draw down occurs, subject to a floor price of $4.95 per common share. Drawdowns will not be permitted on any day when the Conversion Price would be less than this floor price. On the sixth anniversary of the Lenfest Equity Agreement, any issued and outstanding Preferred Stock will be mandatorily converted into ETC common stock at each set Conversion Price. The Lenfest Equity Agreement also allows for us to redeem any outstanding Preferred Stock any time within the six-year term of the Lenfest Equity Agreement. The Preferred Stock will vote with the ETC common stock on an as converted basis. In connection with the execution of the Agreement, the Company drew down $3 million by issuing 3,000 shares of Preferred Stock with a Conversion Price equal to $4.95 per share. Additionally, on July 31, 2006, we drew down an additional $3 million by issuing 3,000 shares of Preferred Stock at a conversion price equal to $6.68 per common share.

On November 16, 2006, we executed an Unsecured Promissory Note (the "Lenfest Note") in favor of Mr. Lenfest in the aggregate principal amount of $3,000,000. Pursuant to the terms of the Lenfest Note, ETC can borrow up to $3,000,000, in increments of $1,000,000, prior to the maturity date of October 6, 2007. As of the date of this filing under Form 10-K, ETC owed $2,000,000 under the Lenfest Note.

All outstanding and unpaid interest on the Lenfest Note is due and payable on the earlier of (i) October 6, 2007 or (ii) such date as ETC draws down funds sufficient to repay the amount due under the Lenfest Note pursuant to the Lenfest Equity Agreement.

Borrowings made pursuant to the Lenfest Note will bear interest at an annual rate of six percent with such interest beginning to accrue on the date of the funding of each loan and, to the extent not paid, compounding on the first day of each month.

The Lenfest Note provides for customary events of default including, but not limited to, the nonpayment of any amount payable when due, certain bankruptcy, insolvency or receivership events and the imposition of certain judgments. Upon the occurrence of an event of default, Mr. Lenfest has the right to accelerate the maturity date of the Lenfest Note and demand immediate payment of all amounts payable there under.

Effective May 9, 2007, the Company entered into a letter agreement with Mr. Lenfest ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

For a more detailed description of the financing provided by Mr. Lenfest and PNC, see the Liquidity and Capital Resources section of the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K and incorporated herein by reference.

Prior to the consummation of the February 19, 2003 refinancing, ATAM, a shareholder and a holder of warrants to purchase 332,820 shares of our common stock, consented to the financing transactions with PNC and Mr. Lenfest including the below market issuance of warrants to Mr. Lenfest. As a result of its consent, ATAM waived, solely in connection with such issuance, the anti-dilution rights contained in its warrant. In exchange for ATAM's consent and waiver, we issued to ATAM warrants to purchase an additional 105,000 shares of common stock. Except for the number of shares issuable upon exercise of the warrants, the new ATAM warrants had substantially the same terms as the warrants issued to Mr. Lenfest. As of the date that these warrants were issued to ATAM, it was the beneficial owner of greater than 5% of our common stock as determined in accordance with Rule 13d-3 under the Securities Exchange Act of 1934. In fiscal year 2005, ATAM exercised all its warrants and received a total of 437,820 shares of our common stock.

Review, Approval or Ratification of Transactions with Related Parties. We have not adopted any formal policies or procedures for the review, approval or ratification of certain related-party transactions. However, such transactions, if and when they are proposed or have occurred, have traditionally been, and will continue to be, reviewed by our Audit Committee on a case-by-case basis. The Audit Committee may consider any relevant factors when reviewing the appropriateness of a related-party transaction, including, but not limited to, the following: (i) the importance of the transaction to ETC; (ii) the amount involved in the proposed transaction; (iii) the specific interest of the director or executive officer (or immediate family members of same) in the proposed transaction; and (iv) the overall fairness of the terms of the transaction to ETC.

Director Independence. The rules of the American Stock Exchange require that a majority of our board of directors be composed of "independent directors," which is defined generally as a person other than an officer or employee of a company or its subsidiaries or any other individual having a relationship, which, in the opinion of the company's board of directors, would interfere with the director's exercise of independent judgment in carrying out the responsibilities of a director. Messrs. Kelley, Gemmill and Anderson are our independent directors and constitute a majority of our board.

Item 14. Principal Accounting Fees and Services

Under the Company's Bylaws and the Charter of the Audit Committee of the Board of Directors, authority to select the Company's auditors rests with the Audit Committee of the Board of Directors. Such selection is made through the formal act of the Audit Committee. It has not been and is not the Company's policy to submit selection of its auditors to the vote of the shareholders because there is no legal requirement to do so. Grant Thornton LLP, an independent registered public accounting firm, was the Company's auditor for the fiscal year ended February 23, 2007. Auditors have not been selected for the current fiscal year. A representative of Grant Thornton is expected to be present at the Annual Meeting and will be given an opportunity to make a statement to the shareholders, if he or she desires to do so. Grant Thornton's representative will also be available to answer appropriate questions from shareholders.

The following table presents fees for professional audit services rendered by Grant Thornton LLP for the audit of the Company's annual financial statements for the fiscal years ended February 23, 2007 and February 24, 2006, respectively, and fees billed for other services rendered by Grant Thornton LLP.

	FY 2007	FY 2006
Audit Fees	$158,862	$152,145
Audit related fees (1)	28,669	44,276
Audit and audit related fees	187,531	196,421
Tax fees (2)	29,721	23,805
Total fees	$217,252	$220,226

(1) Audit related fees consist primarily of employee benefit plan audits.

(2) Tax fees consist of tax compliance services and other consultations on miscellaneous tax matters.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Exhibits:

Number	Item
3.1	Registrant's Articles of Incorporation, as amended, were filed as Exhibit 3.1. to Registrant's Form 10-K for the year ended February 28, 1997 and are incorporated herein by reference.
3.1(i)	Statement with respect to shares of Series B Convertible Preferred Stock, filed as Exhibit 3(i) 1, to Registrant's Form 8-K dated April 6, 2006, and incorporated herein by reference.
3.2	Registrant's amended and restated By-Laws were filed as Exhibit 3.2 to Registrant's Form 8-K dated May 25, 2005, and are incorporated herein by reference.
4.1	$10,000,000 Senior Subordinated Convertible Note, dated February 18, 2003, issued by the Registrant in favor of H.F. Lenfest was filed on February 25, 2003 as Exhibit 4.1 to Form 8-K and is incorporated herein by reference.
10.1	Registrant's 1998 Stock Option Plan was filed on October 8, 1998 on Form S-8 and is incorporated herein by reference. *
10.2	Registrant's Employee Stock Purchase Plan was filed on July 6, 1988 as Exhibit A to the Prospectus included in Registrant's Registration Statement (File No. 33-42219) on Form S-8 and is incorporated herein by reference. *
10.3	Registrant's Stock Award Plan adopted April 7, 1993, was filed as Exhibit 10(ix) to the Registrant's Form 10-K for the fiscal year ended February 25, 1994 and is incorporated herein by reference. *
10.4	Credit Agreement, dated as of February 18, 2003 between the Registrant and PNC Bank, National Association was filed on February 25, 2003 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.5	Amendment to Credit Agreement, dated as of April 30, 2003, between the Registrant and PNC Bank was filed as Exhibit 10.6 to the Registrant's Form 10-K for the fiscal year ended February 28, 2003 and is incorporated herein by reference.
10.6	Amended and Restated Revolving Credit Note, dated April 30, 2003, issued by the Registrant in favor of PNC Bank was filed as Exhibit 10.6 to the Registrant's Form 10-K for the fiscal year ended February 28, 2003 and is incorporated herein by reference.
10.7	Security Agreement, made and entered into as of February 18, 2003, by and between the Registrant, Entertainment Technology Corporation, ETC Delaware, Inc. and PNC Bank was filed on February 25, 2003 as Exhibit 10.3 to Form 8-K and is incorporated herein by reference.
10.8	Pledge Agreement, dated as of February 18, 2003, made by the Registrant in favor of PNC Bank was filed on February 25, 2003 as Exhibit 10.4 to Form 8-K and is incorporated herein by reference.
10.9	Pledge Agreement (Bank Deposits), dated as of February 18, 2003, made by the Registrant in favor of PNC Bank was filed on February 25, 2003 as Exhibit 10.5 to Form 8-K and is incorporated herein by reference.
10.10	Guaranty, dated as of February 18, 2003, made by Entertainment Technology Corporation and ETC Delaware, Inc. in favor of PNC Bank was filed on February 25, 2003 as Exhibit 10.6 to Form 8-K and is incorporated herein by reference.
10.11	Open-End Mortgage and Security Agreement, made as of February 18, 2003, by the Registrant in favor of PNC Bank was filed on February 25, 2003 as Exhibit 10.7 to Form 8-K and is incorporated herein by reference.
10.12	Convertible Note and Warrant Purchase Agreement, dated February 18, 2003, by and between the Registrant and Lenfest was filed on February 25, 2003 as Exhibit 10.8 to Form 8-K and is incorporated herein by reference.
10.13	Registration Rights Agreement, dated as of February 18, 2003, by and between the Registrant and H.F. Lenfest was filed on February 25, 2003 as Exhibit 10.9 to Form 8-K and is incorporated herein by reference.
10.14	Security Agreement, made and entered into as of February 18, 2003, by and among the Registrant, Entertainment Technology Corporation, ETC Delaware, Inc. and H.F. Lenfest was filed on February 25, 2003 as Exhibit 10.10 to Form 8-K and is incorporated herein by reference.
10.15	Guaranty, dated as of February 18, 2003, made by Entertainment Technology Corporation and ETC Delaware, Inc. in favor of H.F. Lenfest was filed on February 25, 2003 as Exhibit 10.11 to Form 8-K and is incorporated herein by reference.

Number	Item
10.16	Open-End Mortgage and Security Agreement, made as of February 18, 2003, by the Registrant in favor of H.F. Lenfest was filed on February 25, 2003 as Exhibit 10.12 to Form 8-K and is incorporated herein by reference.
10.17	Subordination and Intercreditor Agreement, dated as of February 18, 2003, among PNC Bank, H.F. Lenfest and the Registrant was filed on February 25, 2003 as Exhibit 10.13 to Form 8-K and is incorporated herein by reference.
10.18	Amendment to Credit Agreement, dated as of August 24, 2004, between the Registrant and PNC Bank, National Association, was filed on September 10, 2004 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.19	Second Amended and Restated Revolving Credit Note, dated as of August 24, 2004, between the Registrant and PNC Bank, National Association, was filed on September 10, 2004 as Exhibit 10.2 to Form 8-K and is incorporated herein by reference.
10.20	Limited Guaranty Agreement, dated as of August 24, 2004, of H.F. Lenfest in favor of PNC Bank, National Association, was filed on September 10, 2004 as Exhibit 10.3 to Form 8-K and is incorporated herein by reference.
10.21	Amendment to Credit Agreement, dated as of October 18, 2004, between the Registrant and PNC Bank, National Association, was filed on January 10, 2005 as Exhibit 10.1 to Form 10-Q and is incorporated herein by reference.
10.22	Subscription Agreement, dated as of February 14, 2005, between the Registrant and H.F. Lenfest, was filed on February 16, 2005 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.23	2005 Non-employee Director Stock Option Plan, incorporated by reference to Annex A of Registrant's Definitive Proxy Statement on Schedule 14A filed on August 16, 2005 and incorporated herein by reference. *
10.24	Preferred Stock Purchase Agreement between the Registrant and H.F. Lenfest, dated as of April 6, 2006, filed as Exhibit 10.1 to Registrant's Form 8-K dated April 6, 2006, and incorporated herein by reference.
10.25	Registration Rights Agreement between the Registrant and H.F. Lenfest, dated as of April 6, 2006, filed as Exhibit 10.2 to Registrant's Form 8-K dated April 6, 2006, and incorporated herein by reference.
10.26	Amendment to Credit Agreement, dated as of May 18, 2006, between the Registrant and PNC Bank, National Association, was filed on May 23, 2006 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.27	Amendment to Credit Agreement, dated as of June 28, 2006, between the Registrant and PNC Bank, National Association, was filed on June 29, 2006 as Exhibit 10.2 to Form 8-K and is incorporated herein by reference.
10.28	Letter Agreement, dated as of November 16, 2006, between the Registrant and PNC Bank, National Association, was filed on November 20, 2006 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.29	Reimbursement Agreement, dated as of November 16, 2006, between the Registrant and PNC Bank, National Association, was filed on November 20, 2006 as Exhibit 10.2 to Form 8-K and is incorporated herein by reference.
10.30	Restated Subordination and Intercreditor Agreement, dated as of November 16, 2006, between the Registrant and H.F. Lenfest, was filed on November 20, 2006 as Exhibit 10.3 to Form 8-K and is incorporated herein by reference.
10.31	Restated Limited Guaranty Agreement, dated as of November 16, 2006, between the Registrant and H.F. Lenfest, was filed on November 20, 2006 as Exhibit 10.4 to Form 8-K and is incorporated herein by reference.
10.32	Unsecured Promissory Note, dated as of November 16, 2006, between the Registrant and H.F. Lenfest, was filed on November 21, 2006 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.
10.33	Employment Agreement, dated as of November 1, 2005, between Registrant and Duane D. Deaner, Chief Financial Officer. (Filed herewith)*
10.34	Agreement between Registrant and H.F. Lenfest, dated as of May 9, 2007. (Filed herewith)
10.35	Employment Agreement, dated as of July 24, 2006, between Registrant and William F. Mitchell , was filed on July 24, 2006 as Exhibit 10.1 to Form 8-K and is incorporated herein by reference.*
13	Portions of Registrant's 2006 Annual Report to Shareholders which are incorporated by reference into this Form 10-K. (Filed herewith)
14	Code of Ethics. (Filed herewith)
21	Subsidiaries of the Registrant. (Filed herewith)

Number	Item
23	Consent of Grant Thornton LLP. (Filed herewith)
31.1	Certification dated May 24, 2007 pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 made by William F. Mitchell, Chief Executive Officer. (Filed herewith)
31.2	Certification dated May 24, 2007 pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 made by Duane D. Deaner, Chief Financial Officer. (Filed herewith)
32	Certification dated May 24, 2007 pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 made by William F. Mitchell, Chief Executive Officer and Duane D. Deaner, Chief Financial Officer. (Filed herewith)

* Represents a management contract or a compensatory plan or arrangement.

SIGNATURES

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

ENVIRONMENTAL TECTONICS CORPORATION

By /s/ William F. Mitchell
William F. Mitchell,
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, the following persons on behalf of the registrant and in the capacities and on the dates indicated have signed this report below.

Name	Position	Date
/s/ William F. Mitchell William F. Mitchell	Chairman of the Board, Chief Executive Officer, President and Director (Principal Executive Officer)	May 24, 2007
/s/ Duane D. Deaner Duane D. Deaner	Chief Financial Officer (Principal Financial and Accounting Officer)	May 24, 2007
/s/ Howard W. Kelley Howard W. Kelley	Director	May 24, 2007
/s/ H.F. Lenfest H.F. Lenfest	Director	May 24, 2007
/s/ George K. Anderson George K. Anderson, M.D.	Director	May 24, 2007
/s/ Alan M. Gemmill Alan M. Gemmill	Director	May 24, 2007

EXHIBIT INDEX

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EXHIBIT 13

PORTIONS OF
ENVIRONMENTAL TECTONICS CORPORATION
2007
ANNUAL REPORT TO STOCKHOLDERS

FINANCIAL REVIEW
(amounts in thousands, except share and per share information)

Fiscal Year End	2007	2006	2005	2004	2003
Net sales	$ 17,419	$ 25,069	$ 27,814	$ 25,995	$ 43,123
Gross profit	2,071	5,350	6,176	9,943	14,198
Operating (loss) income	(7,932)	(4,719)	(7,130)	131	4,116
Net (loss) income	(8,940)	(6,714)	(8,113)	(793)	2,493
(Loss) earnings per common share:					
Basic	(1.02)	(0.74)	(1.06)	(0.11)	0.35
Diluted	(1.02)	(0.74)	(1.06)	(0.11)	0.33
Working capital	9,708	19,820	29,818	29,907	31,216
Long-term obligations	8,830	8,376	12,087	12,157	12,643
Total assets	31,520	33,667	47,909	48,696	47,698
Total stockholders' equity	14,791	17,553	24,355	25,054	25,907
Weighted average common shares:					
Basic	9,030,000	9,021,000	7,656,000	7,163,000	7,153,000
Diluted	9,030,000	9,021,000	7,656,000	7,163,000	7,497,000

No cash dividends have ever been paid on the Company's common stock, and the Company is prohibited from declaring any cash dividends on its common stock under the terms of its existing credit facilities.

Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are based on the Company's current expectations and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about the Company and its subsidiaries that may cause actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements.

These forward-looking statements include statements with respect to the Company's vision, mission, strategies, goals, beliefs, plans, objectives, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance and business of the company, including but not limited to, (i) projections of revenues, costs of materials, income or loss, earnings or loss per share, capital expenditures, growth prospects, dividends, capital structure, other financial items and the effects of currency fluctuations, (ii) statements of our plans and objectives of the Company or its management or Board of Directors, including the introduction of new products, or estimates or predictions of actions of customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, (iv) statements of assumptions and other statements about the Company or its business, (v) statements made about the possible outcomes of litigation involving the Company; and (vi) statements preceded by, followed by or that include the words, "may," "could," "should," "looking forward," "would," "believe," "expect," "anticipate," "estimate," "intend," "plan," or the negative of such terms or similar expressions. These forward-looking statements involve risks and uncertainties which are subject to change based on various important factors. Some of these risks and uncertainties, in whole or in part, are beyond the Company's control. Factors that might cause or contribute to such a material difference include, but are not limited to, those discussed in the Company's Annual Report on Form 10-K, in the section entitled "Risks Particular to Our Business." Shareholders are urged to review these risks carefully prior to making an investment in the Company's common stock.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

References to fiscal 2007 or the 2007 fiscal year are references to the year ended February 23, 2007. References to fiscal 2008 or the 2008 fiscal year are references to the year ending February 29, 2008.

Overview

We are principally engaged in the design, manufacture and sale of software driven products and services used to recreate and monitor the physiological effects of motion on humans and equipment and to control, modify, simulate and measure environmental conditions. These products include aircrew training systems (aeromedical, tactical combat and general), disaster management systems and services, entertainment products, sterilizers (steam and gas), environmental testing products and hyperbaric chambers and other products that involve similar manufacturing techniques and engineering technologies. We operate in two primary business segments, the Training Services Group (TSG) (formerly Aircrew Training Systems (ATS)) and the Control Systems Group (CSG) (formerly the Industrial Group (IG)).

The following factors had an adverse impact on our performance for the fiscal year ended February 23, 2007:

- continued unfavorable global economic and political conditions for our aeromedical products;
- the cost of development and marketing efforts for our Authentic Tactical Fighting Systems;
- spending to modify our main facility in Southampton, Pa., and to build equipment for the National Aerospace Training and Research (NASTAR) Center.

Historically our ATS open contract mix has included one large order (e.g., a centrifuge or an order for an entire training center of equipment), a few medium-priced simulators, and other low-end trainers. Large dollar contracts have tended to be received every 18 months to two years, although some significant events such as September 11, 2001, and the current conflict in Iraq have disrupted this cycle. The ATS product line is especially sensitive to global economic and political pressures including anti-American sentiment. Fiscal 2007 saw a continuation of the new contract delays due to budget constraints and other issues of our customers located throughout the world. Most of our ATS sales are to international government defense customers.

In response to the ongoing market budgetary constraints for G-force training and spatial disorientation, in 2004 we began incorporating tactical combat flight capabilities into our centrifuge technology. Dubbed the Authentic Tactical Fighting System, this product was the first fully "flyable" centrifuge-based tactical maneuvering ground based simulator. This technology allows a fighter pilot to practice tactical air combat maneuvers such as dodging enemy missiles, ground fire and aircraft obstacles while experiencing the real life environment of a high G-force fighter aircraft. These flight trainers provide a low cost and extremely less risky alternative to actual air flight. We continued development of this technology through fiscal 2007.

A second and equally complicated challenge has been marketing tactical flight simulation to the world's defense agencies. This new technology is contrary to the conventional training belief that tactical flight and combat skills can only be learned in a flying aircraft. In January 2007 we achieved a major milestone in that the U.S. Air Force Research Lab prepared a business plan which incorporated the funds to build a joint strike fighter cockpit for the ATFS-400 simulator. This is the first step towards testing and validation of this technology by the U.S. military.

Our third major challenge in this re-engineering of our aeromedical business has been a shifting of our business model. In fiscal 2006, we began construction of the National Aerospace Training and Research (NASTAR) Center. This center, set to open in fiscal 2008, is an integrated pilot training center offering a complete range of aviation training and research support for military jet pilots and civil aviation as well as space travel and tourism. The NASTAR Center will house state of the art equipment including the ATFS-400, a GYROLAB GL-2000 Advanced Spatial Disorientation Trainer, a Hypobaric Chamber, an Ejection Seat Trainer, and a Night Vision and Night Vision Goggle Training System. These products represent 37 years of pioneering development and training solutions for the most rigorous stresses encountered during high performance aircraft flight including the effects of altitude exposure, High G-force exposure, spatial disorientation and escape from a disabled aircraft.

- continued development of generation 3 software for our Advanced Disaster Management Scenario product line;
- spending to investigate and evaluate the best way to offer disaster training services;

We have made significant progress in advancing and enhancing our ADMS line of products. Graphics are sharper and more realistic, interactivity and connectivity of objects is tighter, additional disaster scenarios have been added, and we have made the hardware configuration more user friendly. In fiscal 2007 we completed development of our third generation software platform and determined the direction for generation 4, which effort will begin in fiscal 2008. Concurrently, we contracted marketing studies to evaluate the best way to sell simulation training. The result was a decision to migrate to a services-based approach. Consistent with this change in strategy, in April 2007 we appointed Mr. Marco van Wijngaarden as president of this division. Mr. van Wijngaarden has been the head of training for the Netherlands' National Institute for Safety, a major ADMS user, and is very familiar with the ADMS product line. Continued development of the product and business put pressure on operating results for fiscal 2007.

- limited revenue generation coupled with high development costs in our low-end entertainment products;

Certain actions by a former major entertainment customer have effectively closed the high-end amusement market to us. Our low-end products have encountered customer resistance due to pricing and those units under a revenue share contract have failed to generate sufficient income to justify an expansion of this line. Consequently, this line has suffered from high development costs with low return. We consider this line to be an opportunistic business and will plan our development accordingly.

- development costs to further enhance the functionality of our GL-2500 GYROLAB product;

This development was performed under a contract for a customer in Japan. The cost of many new features was only partially covered by the contract value, resulting in a slim gross profit for the contract.

- higher costs of capital and amortization of deferred finance charges;

Interest expense for fiscal 2007 was $1,277,000 or 7.3% of sales. This included approximately $454,000 of non-cash charges for amortization of debt discount expenses.

- public company and litigation and claims costs;

These two categories of expenses accounted for almost 22% of our selling and administrative expenses and totaled over 11% of sales. Our two significant legal cases are both expected to be resolved in fiscal 2008.

- cash flow;

One of the greatest challenges we faced was adequately funding the cash requirements of large, long-term multi-year projects, the costs of technological development of existing products, the cost to modify the building and produce the equipment for the NASTAR Center, and the costs to market our ATFS technology to the U.S. government and international government defense agencies. Although some long-term contracts incorporate milestone payments, the cash flows associated with production and material requirements tend to vary significantly over time. These projects are usually cash positive in the early stages and cash negative during the production phase. Funding these contracts and the other initiatives throughout the year required a significant amount of operating funds. Since our bank facility was restricted to use for letters of credit, we were forced to negotiate alternate financial agreements with Mr. Lenfest, a member of the board of Directors. On April 7, 2006, we entered into a Preferred Stock Purchase Agreement which permitted ETC under certain circumstances to draw down up to $15 million, and on November 16, 2006, we signed an Unsecured

Promissory Note for $3 million, both with Mr. Lenfest. (As of the date of this filing on Form 10-K, we had $9 million and $1 million still available, respectively, under the two agreements.) Both agreements expire on October 6, 2007. Also on November 16, 2006, we entered into a Letter Agreement with PNC Bank. This Letter Agreement amended, restated and replaced the existing PNC Credit Agreement. Pursuant to such agreement, PNC Bank (i) terminated our Credit Agreement dated as of February 18, 2003 (ii) re-approved our $5 million Line of Credit for Letters of Credit, and (iii) re-affirmed the Tangible Net Worth covenant (as defined in the Agreement) to be a minimum of $9,000,000. The $5 million Line of Credit for Letters of Credit continued to be guaranteed by Mr. Lenfest. As of February 23, 2007, we had used approximately $2,607,000 of the availability under the PNC Agreement for international letters of credit.

Effective May 9, 2007, the Company entered into a letter agreement with Mr. Lenfest ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

We have recently noticed renewed customer interest in some significant international aeromedical proposals. These proposals have favorable payment terms including down payments. Although it cannot be predicted when and if any of these contracts might actually be awarded, they are another potential source of operating funds.

Given our low beginning sales backlog and ongoing difficulty in obtaining new contracts, we may need to obtain additional sources of capital in order to continue growing and operating our business. Because we have established businesses in many markets, own significant fixed assets including a building, and other business assets which can be used for security, we believe that we will be able to locate such additional sources of capital, although there is no assuredness that we will be successful in this endeavor.

We face the following challenges and business goals in order to make fiscal 2008 a successful year:

- Complete the building modifications and equipment production and open the NASTAR Center.
- Book at least one significant training contract for the NASTAR Center. This could be in the area of pilot training, aeromedical research or space adventure.
- Book an order for cockpits for the ATFS-400 for either the U.S. Navy or the U.S. Air Force.
- Begin validation of the ATFS technology.
- Book at least one significant international contract for aeromedical equipment.
- Successfully execute the open large order for environmental control equipment booked near the end of fiscal 2007.
- Design and implement an awareness program to introduce and educate alternative hyperbaric medicine applications users in the applicability, functionality and flexibility of our hyperbaric monoplace chamber.
- Maximize sales bookings in our sterilizer division.
- Complete and implement our new training services business plan in our ADMS line.
- Finalize our two outstanding major litigation cases either through settlement, mediation or by judicial determination.
- In ETC-PZL, replace the recently completed significant contract from L-3 Communications with additional outside contracts.
- Restructure or replace our existing letter of credit facility with PNC and our financial borrowing arrangements with Mr. Lenfest. The PNC Agreement expires in June, 2007, and both the Lenfest Equity Line and the Promissory Note expire in October 2007.

Our plans to meet our goals include the following:

- Market ATFS technology to the U.S. military.
- Market our ability to provide aeromedical training for potential passengers for space sub-orbital flight.
- Reduce our costs of manufacture for all product offerings in our Control Systems Group divisions.
- Design and implement an awareness program to introduce and educate alternative hyperbaric medicine applications users in the applicability, functionality and flexibility of our hyperbaric monoplace chamber.
- Negotiating with a potential bank to establish a line of credit which will either replace or supplant our existing equity line and unsecured note with Mr. Lenfest.

Revenue Recognition

We currently market our products and services primarily through our sales offices and employees. In addition, we also utilize the services of approximately 100 independent sales agents and organizations in seeking foreign orders for our products.

We sell utilizing two business approaches: integrated training services and products. Some of our products are customized, using our proprietary software based on specifications provided by our customers. Some of our products take more than one year to manufacture and deliver to the customer. In the TSG segment, we offer integrated training services to both commercial and government military defense agencies and training devices to government military defense agencies both in the United States and internationally. We sell our entertainment products to amusement parks, zoos and museums. We sell our disaster management simulation training and products to fire and emergency training schools and state and local governments. In the CSG segment, we sell our sterilizers to pharmaceutical and medical device manufacturers. We sell our environmental testing systems primarily to commercial automobile manufacturers and heating, ventilation and air conditioning (HVAC) manufacturers. We sell our hyperbaric products to the military (mainly larger chambers) and hospitals and clinics (mainly single occupant monoplace chambers). To a lesser degree, we provide upgrade, maintenance and repair services for our products and for products manufactured by other parties.

We recognize revenue using three methods:

On long-term contracts over $250,000 in value and over six months in length, the percentage of completion (POC) revenue recognition method is utilized. Under this method a percentage is calculated based on costs incurred from inception to date on a contract as compared to the estimated total costs required to fulfill the contract. This percentage is then multiplied by the contract value to determine the amount of revenue to be recognized in any given accounting period. Revenue recognized on uncompleted long-term contracts in excess of amounts billed to customers is reflected as a current asset on the balance sheet under the caption “costs and estimated earnings in excess of billings on uncompleted long-term contracts”. Amounts billed to customers (milestone payments) in excess of revenue recognized are reflected as a current liability on the balance sheet under the caption “billings in excess of costs and estimated earnings on uncompleted long-term contracts.” At any time during performance if it is estimated that a contract at completion will result in a loss, the entire amount of the estimated loss is accrued. The effect of revisions in cost and profit estimates for long-term contracts is reflected in the accounting period in which we learn the facts which require us to revise our cost and profit estimates. Contract progress billings are based upon contract provisions for customer advance payments, contract costs incurred, and completion of specified contract milestones. Contracts may provide for customer retainage of a portion of amounts billed until contract completion. Retainage is generally due within one year of completion of the contract. Revenue recognition under the percentage of completion method involves significant estimates, both at inception and throughout the performance period.

Revenue for contracts under $250,000, or to be completed in less than six months, and where there are no post-shipment services (such as installation and customer acceptance) is recognized on the date that the finished product is shipped to the customer.

Revenue for the sale of parts and services is also recognized on the date that the part is shipped to the customer or when the service is completed. Revenue for service contracts is recognized ratably over the life of the contract with related material costs expensed as incurred.

In accordance with accounting principles generally accepted in the United States of America, recognizing revenue on contract claims and disputes related to customer caused delays, errors in specifications and designs, and other unanticipated causes, for amounts in excess of contract value, is appropriate if it is probable that the claim will result in an increase in the contract value and if the company can reliably estimate the amount of potential additional contract revenue (claim revenue). However, revenue recorded on a contract claim cannot exceed the incurred contract costs related to that claim. Claims are subject to negotiation, arbitration and audit by the customer or governmental agency.

We have operating subsidiaries in the United Kingdom and Poland, maintain regional offices in the Middle East, Asia and Canada, and use the services of approximately 100 independent sales organizations and agents throughout the world. ETC International Corporation is a holding company established for federal income tax purposes and is not an operating subsidiary. We consider our business activities to be divided into two segments: the Training Services Group (TSG) and the Control Systems Group (CSG). The TSG includes aircrew training products and services, disaster management training product and services and entertainment products. The CSG includes sterilizer, environmental and hyperbaric products and services.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that reflect significant judgments and uncertainties and potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies include those described below. For a detailed discussion on the application of these and other accounting policies, see Note 3 to the Consolidated Financial Statements, Summary of Significant Accounting Policies.

Revenue Recognition on Long-Term Contracts

On long-term contracts over $250,000 in value and over six months in length, the percentage of completion (POC) revenue recognition method is utilized. If we do not accurately estimate the total cost required to fulfill the contract, or if we are unsuccessful in the ultimate collection of any associated contract claims, estimated gross margins may be significantly impacted or losses may need to be recognized in future periods. Any resulting reductions in margins or contract losses could be material to our results of operations and financial position.

Accounts Receivable

We perform ongoing credit evaluations of our customers and adjust credit limits based on payment history and the customer’s current creditworthiness. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based on historical experience and any specific customer collection issues that have been identified. Most of our collection issues are related to contract disputes, not customer creditworthiness. While our credit losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. Additionally, as a result of the concentration of international receivables, we cannot predict the effect, if any, that geopolitical disputes and financial constraints will have on the ultimate collection of our international receivables.

In accordance with accounting principles generally accepted in the United States of America, recognizing revenue on contract claims and disputes related to customer caused delays, errors in specifications and designs, and other unanticipated causes, for amounts in excess of contract value, is appropriate if it is probable that the claim will result in an increase in the contract value and if the company can reliably estimate the amount of potential additional contract revenue (claim revenue). However, revenue recorded on a contract claim cannot exceed the incurred contract costs related to that claim. Claims are subject to negotiation, arbitration and audit by the customer or governmental agency.

Results of Operations

We have historically experienced significant variability in our quarterly revenue, earnings and other operating results, and our performance may fluctuate significantly in the future.

Fiscal 2007 versus Fiscal 2006

(amounts in thousands)

	Summary Table of Results			
	Year ended February 23, 2007	Year ended February 24, 2006	Variance $ ( ) = Unfavorable	Variance %
Sales:				
Domestic	$ 6,012	$ 9,140	$ (3,128)	(34.2)%
US Government	586	2,586	(2,000)	(77.3)%
International	10,821	13,343	(2,522)	(18.9)%
Total Sales	17,419	25,069	(7,650)	(30.5)%
Gross Profit	2,071	5,350	(3,279)	(61.3)%
Selling, general & administrative	9,434	9,625	191	2.0%
Research & development	569	422	(147)	(34.8)%
Impairment expense	—	22	22	—
Operating loss	(7,932)	(4,719)	(3,213)	68.1%
Interest expense, net	1,151	1,857	706	38.0%
Other expense, net	(58)	(15)	43	(286.7)%
Income taxes	(77)	136	213	156.6%
Minority interest	(8)	17	25	147.1%
Net loss	$ (8,940)	$ (6,714)	$ (2,226)	(33.2)%
Net loss per common share	$ (1.02)	$ (0.74)	$ (0.28)	(37.8)%

Net Loss.

ETC had a net loss of $8,940,000 or $(1.02) per share (diluted) in fiscal 2007 versus a net loss of $6,714,000 or $(0.74) per share (diluted) in fiscal 2006, an increase in net loss of $2,226,000 or 33.2%. Operating loss was $7,932,000 versus an operating loss of $4,719,000 in 2006, an increase in operating loss of $3,213,000 or 68.1%.

The increase in operating loss resulted from decreased gross profit and increased research and development expenses which were only partially offset by reduced selling, general and administrative expenses. Net loss in fiscal 2007 included an income tax benefit in ETC-PZL, the Company's Polish subsidiary. Net loss in fiscal 2006 did not reflect an income tax benefit. (See "Benefits from/Provision for Income Taxes.")

Sales.

For the fiscal year ended February 23, 2007, total sales were $17,419,000, a decrease of $7,650,000 or 30.5% from fiscal 2006. The reduction was approximately equally split between ETC Southampton (down $3,657,000 or 18.6%) and ETC-PZL (down $3,801,000 or 73.4%). Product line sales in ETC Southampton in the current period were down in three product categories (environmental, down $2,105,000, Pilot Training Systems (PTS), down $2,075,000, and parts and service, down $255,000), with partial offsets primarily in sterilizers (up $466,000) and simulation (up $186,000). Reduced sales in environmental reflected a significant decrease in domestic automotive sales. The decrease in PTS sales reflected significant production activity in the prior period for a pilot selection system purchased through the U.S. Army Corp of Engineers for a Middle Eastern country. Parts and service suffered from a reduction in domestic activity. Sterilizer sales benefited from a significant increase in international contracts which was only partially offset by a decrease domestically. Simulation reflected higher domestic sales. ETC-PZL reflected reduced production on the L-3 simulator contract.

Geographically, domestic sales were $6,012,000, down $3,128,000, or 34.2%, from fiscal 2006, and represented 34.5% of total sales, down from 36.5% in fiscal 2006, reflecting reduced activity in most product categories. Reflecting the aforementioned U.S. Army Corp of Engineers project, U.S. government sales decreased to $586,000, as compared to $2,586,000 in fiscal 2006, and represented 3.4% of total sales, down from 10.3% in fiscal 2006. International sales, including those in the Company's foreign subsidiaries, were

$10,821,000, down $2,522,000 or 18.9%, and represented 62.1% of total sales, up from 53.2% in fiscal 2006, as an increase in ETC Southampton international sales (primarily sterilizers) was completely offset by the aforementioned significant reduction in ETC-PZL. Throughout our history, most of the sales for ATS products have been made to international customers.

In fiscal 2007, one customer represented individually 10% or more of total sales, Jupitor (Japan), which generated $3,365,000 or 19.3% of total sales. International sales totaling at least $500,000 per country were made to customers in Japan, Australia and Pakistan. Fluctuations in sales to international countries from year to year primarily reflect percentage of completion revenue recognition on the level and stage of development and production on multi-year long-term contracts. Open orders for one international and one domestic customer represented 43.9% of our backlog at February 23, 2007. For a discussion of the additional risks associated with our international operations, see “Risks Particular to Our Business—There are certain risks inherent in our international business activities, which constitute a significant portion of our business,” in our Annual Report on Form 10-K.

We have historically experienced significant variability in our sales performance. This reflects the existing sales backlog, product and the nature of contract (size and performance time) mix, the manufacturing cycle and amount of time to effect installation and customer acceptance, and certain factors not in our control such as customer delays and the time required to obtain U.S. Government export licenses. One or a few contract sales may account for a substantial percentage of our revenue in any period.

Domestic Sales.

Overall, domestic sales in fiscal 2007 were $6,012,000 as compared to $9,140,000 in fiscal 2006, a decrease of $3,128,000 or 34.2%, reflecting reduced activity in most product categories. Most significantly, environmental reflected a significant decrease in domestic automotive sales while the sterilizer division saw a shift to international contracts. Domestic sales represented 34.5% of our total sales in fiscal 2007, down from 36.5% in fiscal 2006. Sales to the U.S. Government in fiscal 2007 were $586,000 as compared $2,586,000 in fiscal 2006, and represented 3.4% of total sales in fiscal 2007 versus 10.3% in fiscal 2006.

International Sales.

International sales in fiscal 2007, including those in our foreign subsidiaries, were $10,821,000 as compared to $13,343,000 in fiscal 2006, a decrease of $2,522,000 or 18.9%, but represented 62.1% of total sales as compared to 53.2% in fiscal 2006. Throughout our history, most of the sales for ATS have been made to international customers. In fiscal 2007, international sales totaling at least ten percent of total international sales were made to a customer in Japan ($3,365,000) and to two customers in Australia (totaling $1,374,000). In fiscal 2006, international sales totaling at least ten percent of total international sales were made in ETC-PZL to L-3 Communications ($4,599,000) and to a government customer in Pakistan ($2,910,000). Fluctuations in sales to international countries from year to year primarily reflect revenue recognition on the level and stage of development and production on multi-year long-term contracts.

Segment Sales.

($000 except for %).

Fiscal	Training Services Group		Control Systems Group		Total	
Year	$	%	$	%	$	%
2007	9,293	53.3%	8,126	46.7%	17,419	100.0%
2006	15,100	60.2%	9,969	39.8%	25,069	100.0%

On a segment basis, sales of our TSG products, most of which create and monitor the physiological effects of motion (including spatial disorientation and centrifugal forces) on humans and equipment for medical, training, research and entertainment markets, were $9,293,000 in fiscal 2007, a decrease of $5,807,000, or 38.5% from fiscal 2006. Sales of these products accounted for 53.3% of our sales versus 60.2% in fiscal 2006. Sales in our other segment, CSG, which designs and produces chambers that create environments that are used for sterilization, research and medical applications, decreased $1,843,000 to $8,126,000, a decrease of 18.5%, and constituted 46.7% of our total sales compared to 39.8% in fiscal 2006.

Significant claims outstanding at February 23, 2007 and February 24, 2006 included a claim with the U.S. Government for a submarine decompression chamber ($3.0 million recorded). We have settled two international claims in recent fiscal years. On February 8, 2005, we reached an agreement totaling $4.7 million on an international claim and effective February 27, 2004 we reached an agreement totaling $10.5 million on another international claim. Although recorded as a current asset in the financial statements, all remaining claim revenues may not be received in full during fiscal 2008. For a more complete discussion of outstanding claims, see “Note 4. Accounts Receivable” to our consolidated financial statements in the Annual Report to Stockholders following.

Gross Profit.

Gross profit for fiscal 2007 decreased by $3,279,000 or 61.3% from fiscal 2006 reflecting the sales decrease and a 9.4 percentage point decrease in the gross profit rate as a percent of sales. The dollar decrease primarily resulted from the aforementioned sales reductions in ETC Southampton which also was the primary contributor to the rate decrease. PTS, environmental and sterilizers all

experienced reduced rates. PTS suffered due to additional development work performed in the current period on the Jupitor GYROLAB contract and also reflected an unfavorable comparison to the prior period which included significant production for a higher gross profit contract from the U.S. Army Corp of Engineers for a Middle Eastern country. The environmental gross profit rate reflected a cost overrun on a domestic automotive project. Sterilizers had reduced rates for domestic work. ETC-PZL had reduced gross profit dollars on the reduced sales activity.

Selling and Administrative Expenses.

Selling and administrative expenses decreased $191,000, or 2.0%, from fiscal 2006, although the rate as a percent of sales increased from 38.5% in fiscal 2006 to 54.2% in fiscal 2007. The major dollar differences between the periods were reduced commissions on reduced sales and a higher mix of non-commissionable sales, lower bad debt expense, and lower claims expenses. Three types of spending in this expense category, sales commissions, claim costs, and public company related expenses, accounted for approximately 28% of total selling and administrative expenses in the current period.

Research and Development Expenses.

Research and development expenses increased $147,000 or 34.8% in fiscal 2007 as compared to fiscal 2006. This increase reflected reduced reimbursement for government grants in our Turkish subsidiary under government research awards. Most of our research efforts, which were and continue to be significant costs of our business, are included in cost of sales for applied research for specific contracts, as well as research for feasibility and technology updates. Capitalized software development costs for fiscal 2007 were $537,000 compared to $489,000 in fiscal 2006. Amortization of software costs, which was charged to cost of sales, was $1,231,000 and $1,224,000 for fiscal 2007 and fiscal 2006, respectively.

Operating Loss.

Operating loss was $7,932,000 compared to an operating loss of $4,719,000 in 2006, an increase in loss of $3,213,000 or 68.1%, reflecting the aforementioned reduced gross profit partially offset by reduced selling and administrative expenses.

On a segment basis, TSG had an operating loss of $3,991,000, an increase of $436,000 or 12.3% over fiscal 2006, while the CSG had an operating loss of $2,724,000 in fiscal 2007, an increase in operating loss of $2,362,000 from fiscal 2006. These segment operating results were offset, in part, by unallocated corporate expenses of $1,217,000, an increase of $415,000 from fiscal 2006.

The increase in operating loss for the TSG segment in fiscal 2007 reflected lower sales and corresponding gross profit compared to fiscal 2006.

The CSG segment's increased operating loss in fiscal 2006 reflected a lower gross margin and a sales decrease.

Interest Expense.

Interest expense (net of interest income) decreased $706,000 or 38.0% in fiscal 2007 from fiscal 2006. The prior period included significant non-cash charges for amortization of deferred financing costs from our previous refinancing, amortization of debt discount resulting from the additional warrants issued to Mr. Lenfest in exchange for his guarantee on a portion of the bank facility in August 2004 and interest expense on our long-term bonds which were redeemed on August 1, 2005.

Other Income, net.

Other income, net, increased $43,000 for fiscal 2007 versus fiscal 2006 reflecting higher exchange gain in our Polish subsidiary, ETC-PZL coupled with lower bank fees and letter of credit charges.

(Benefit from)/Provision for Income Taxes.

Income tax benefit in fiscal 2007 resulted from applying in ETC-PZL carry-loss forwards to offset current income taxes due on pre-tax earnings (although ETC-PZL had a book loss for reporting purposes, it reported a profit for tax purposes) and from recording a tax benefit on the pre-tax book loss. Although ETC Southampton reported a pre-tax loss during fiscal 2007, no offsetting income tax benefit and corresponding deferred tax asset was recorded, due to the uncertain nature of their ultimate realization based on past performance and the potential that sufficient taxable income may not be generated in the near future. We will recognize these benefits only as reassessment demonstrates that they are realizable. Realization is entirely dependent upon future earnings in specific tax jurisdictions.

Income tax expense in fiscal 2006 represented income taxes on pre-tax earnings in ETC-PZL and the establishment of a reserve for prior income tax benefits accrued on intercompany transactions losses. During fiscal 2006, we applied for and received refunds approximating $580,000.

Reflecting the Company's significant losses in the current and prior fiscal years, the Company has approximately $20.5 million of federal net loss carry forwards available to offset future income tax liabilities, beginning to expire in 2025. However,

due to the uncertain nature of their ultimate realization based on past performance, and the potential that sufficient taxable income may not be generated in the near future, we have established a full valuation allowance of the same amount against these carry forward benefits and will recognize these benefits only as reassessment demonstrates that they are realizable. Realization is entirely dependent upon future earnings in specific tax jurisdictions. While the need for this valuation allowance is subject to periodic review, if the allowance is reduced, the tax benefits of the carry forwards will be recorded in future operations as a reduction of our income tax expense. In addition, the Company may be subject to limitation on the use of its net operating losses based on the potential ownership change that may have occurred as defined by Section 382 of the Internal Revenue Code. The Company is currently evaluating the need to undertake an ownership change study in order to conclude if a further limitation is required.

Fiscal 2006 versus Fiscal 2005

Summary Table of Results

	Year ended February 24, 2006 (amounts in thousands)	Year ended February 25, 2005	Variance $	Variance %
			( ) = Unfavorable	
Sales:				
Domestic	$ 9,140	$ 11,998	$(2,858)	(23.8%)
US Government	2,586	2,904	(318)	(11.0%)
International	13,343	12,912	431	3.3%
Total Sales	25,069	27,814	(2,745)	(9.9%)
Gross Profit	5,350	6,176	(826)	(13.4%)
Selling, general & administrative	9,625	12,450	2,825	22.7%
Research & development	422	856	434	50.7%
Impairment expense	22	—	(22)	n/a
Operating loss	(4,719)	(7,130)	2,411	33.8%
Interest expense, net	1,857	1,792	(65)	(3.6%)
Other expense, net	7	308	301	97.7%
Income taxes	136	(1,117)	(1,253)	(1,021.3%)
Minority Interest	17	—	(17)	n/a
Net loss	$ (6,714)	$ (8,113)	$ 1,399	17.2%
Net loss per common share	$ (0.74)	$ (1.06)	$ 0.32	30.2%

Net Loss.

ETC had a net loss of $6,714,000 or $(0.74) per share (diluted) in fiscal 2006 versus a net loss of $8,113,000 or $(1.06) per share (diluted) in fiscal 2005, an improvement of $1,399,000 or 17.2%. Operating loss was $4,719,000 versus an operating loss of $7,130,000 in 2005, an improvement of $2,411,000 or 33.8%. The improvement in operating loss resulted from lower selling, general and administrative costs and research and development costs which were only partially offset by reduced gross profit. Net loss in fiscal 2006 did not have any income tax benefit offset. (See "Provision for/Benefit from Income Taxes.")

Sales.

For the fiscal year ended February 24, 2006, total sales were $25,069,000, a decrease of $2,745,000 or 9.9% from fiscal 2005. The reduction reflected a significant ($7,041,000, 26.3%) decrease in our domestic operation which was only partially offset by a correspondingly significant ($4,417,000, 577.4%) increase in our Polish subsidiary, ETC-PZL. Product line sales in ETC Southampton in the current period were down in all categories except sterilizers versus the prior period. The decrease in Training System Group (TSG) (formerly known as Aircrew Training Systems (ATS)), sales in ETC Southampton ($4,327,000, 32.6%) reflected completion of a centrifuge device for Malaysia in the prior period and revenue for the aforementioned claim settlement. Hyperbaric was down reflecting, again in the prior period, the near completion of two large chambers destined for a Middle Eastern navy. Entertainment was down $1,168,000, 85.6%, reflecting reduced sales of the Wild Earth amusement ride. The increase in sterilizers ($1,522,000, 82.6%) primarily reflected increased sales for mid-size steam units.

Geographically, domestic sales were $9,140,000, down $2,858,000, or 23.8%, from fiscal 2005, and represented 36.5% of total sales, down from 43.1% in fiscal 2005, primarily reflecting reduced activity for hyperbaric, entertainment and PTS. U.S. government sales decreased to $2,586,000, as compared to $2,904,000 in fiscal 2005, and represented 10.3% of total sales, down from 10.4% in fiscal 2005. International sales, including those in the Company's foreign subsidiaries, were $13,343,000, up $431,000 or

3.3%, and represented 53.2% of total sales, up from 46.4% in fiscal 2005, primarily reflecting significantly increased sales in ETC-PZL. Throughout our history, most of the sales for ATS products have been made to international customers.

In fiscal 2006, two customers represented individually 10% or more of total sales, L-3 Communications and the Pakistan Air Force, which together generated $7,509,000 or 30% of total sales. International sales totaling at least $500,000 per country were made to customers in Pakistan, Japan and China. Fluctuations in sales to international countries from year to year primarily reflect percentage of completion revenue recognition on the level and stage of development and production on multi-year long-term contracts. Open orders for two international customers and one domestic customer represented 47.4% of our backlog at February 24, 2006. For a discussion of the additional risks associated with our international operations, see “Risks Particular to Our Business—There are certain risks inherent in our international business activities, which constitute a significant portion of our business,” in our Annual Report on Form 10-K.

We have historically experienced significant variability in our sales performance. This reflects the existing sales backlog, product and the nature of contract (size and performance time) mix, the manufacturing cycle and amount of time to effect installation and customer acceptance, and certain factors not in our control such as customer delays and the time required to obtain U.S. Government export licenses. One or a few contract sales may account for a substantial percentage of our revenue in any period.

Domestic Sales.

Overall, domestic sales in fiscal 2006 were $9,140,000 as compared to $11,998,000 in fiscal 2005, a decrease of $2,858,000 or 23.8%, reflecting reduced activity for all product types except sterilizers. Most significantly, hyperbaric (down $1,828,000, 67.6%) suffered from the near completion in the prior year period on a POC revenue basis of a contract for two large chambers destined for a foreign navy. Entertainment sales were down from the prior period as fiscal 2005 reflected significant revenue for the first year orders of “Wild Earth” and “Monster Truck” amusement rides. ATS product line sales were down as the prior period included a sale of a Gyro-IPT. Domestic sales represented 36.5% of our total sales in fiscal 2006, down from 43.1% in fiscal 2005. Sales to the U.S. Government in fiscal 2006 were $2,586,000 as compared $2,904,000 in fiscal 2005, and represented 10.3% of total sales in fiscal 2006 versus 10.4% in fiscal 2005.

International Sales.

International sales in fiscal 2006, including those in our foreign subsidiaries, were $13,343,000 as compared to $12,912,000 in fiscal 2005, an increase of $431,000 or 3.3%, and represented 53.2% of total sales as compared to 46.4% in fiscal 2005. Throughout our history, most of the sales for ATS have been made to international customers. In fiscal 2006, international sales totaling at least ten percent of total international sales were made in our Polish subsidiary to L-3 Communications ($4,599,000) and to a government customer in Pakistan ($2,910,000). In fiscal 2005, international sales totaling at least ten percent of total international sales were made to government or commercial accounts in Malaysia ($3,388,000) and Egypt ($2,309,000). Fluctuations in sales to international countries from year to year primarily reflect revenue recognition on the level and stage of development and production on multi-year long-term contracts.

Segment Sales.

($000 except for %)

Fiscal Year	Training Services Group (formerly ATS) $	%	Control Systems Group (formerly IG) $	%	Total $	%
2006	15,100	60.2%	9,969	39.8%	25,069	100.0%
2005	16,787	60.3%	11,027	39.7%	27,814	100.0%

On a segment basis, sales of our TSG products, which create and monitor the physiological effects of motion (including spatial disorientation and centrifugal forces) on humans and equipment for medical, training, research and entertainment markets, were $15,100,000 in fiscal 2006, a decrease of $1,687,000, or 10.1% from fiscal 2005. Sales of these products accounted for 60.2% of our sales versus 60.3% in fiscal 2005. Sales in our other segment, CSG (formerly the Industrial Group), which designs and produces chambers that create environments that are used for sterilization, research and medical applications, decreased $1,058,000 to $9,969,000, a decrease of 9.6%, and constituted 39.8% of our total sales compared to 39.7% in fiscal 2005.

Significant claims outstanding at February 24, 2006 and February 25, 2005 included a claim with the U.S. Navy for a submarine decompression chamber ($3.0 million recorded). We have settled two international claims in the last two fiscal years. On February 8, 2005, we reached an agreement totaling $4.7 million on an international claim and effective February 27, 2004 we reached an agreement totaling $10.5 million on another international claim. Although recorded as a current asset in the financial statements, all remaining claim revenues may not be received in full during fiscal 2007. For a more complete discussion of outstanding claims, see “Note 3. Accounts Receivable” to our consolidated financial statements in the Annual Report to Stockholders following.

Gross Profit.

Gross profit for fiscal 2006 decreased by $826,000 or 13.4% from fiscal 2005 reflecting the sales decrease and a slight (0.9 percentage point) decrease in the gross profit rate as a percent of sales. The dollar decrease primarily resulted from the aforementioned sales reductions in our domestic operation's TSG, hyperbaric and entertainment product areas coupled with an increase in inventory reserves. The reduction in the rate as a percent of sales primarily reflected reduced margin performance in ETC-PZL and the impact of additional reserves as the margin rates for most product areas in our domestic operation were favorable versus the prior period, most significantly double digit increases in environmental, PTS and simulation. Acting as a partial offset was increased gross profit dollars at a slightly better rate. This improvement reflected the aforementioned significant increase in sales primarily for mid-sized steam units. Both PTS and simulation margin performance reflected continued additional product development costs, both to enhance functionality of existing products and to develop product extensions, which negatively impacted gross profit as these costs are primarily charged directly to the cost of sales for specific orders.

Selling and Administrative Expenses.

Selling and administrative expenses decreased $2,825,000, or 22.7%, from fiscal 2005. The major difference during the periods was reduced legal and claim expenses. During fiscal 2005, we incurred significant legal costs and claims expenses to support an international claim which was settled on February 8, 2005. Acting as a partial offset were additional bad debt reserves. As a percentage of sales, selling and administrative expenses were 38.4% in fiscal 2006 compared to 44.8% in fiscal 2005.

Research and Development Expenses.

Research and development expenses decreased $434,000 or 50.7% in fiscal 2006 as compared to fiscal 2005. This decrease reflected both reduced spending and the timing of reimbursement for government grants in our Turkish subsidiary under a government research award for two projects. Most of our research efforts, which were and continue to be a significant cost of our business, are included in cost of sales for applied research for specific contracts, as well as research for feasibility and technology updates. Capitalized software development costs for fiscal 2006 were $850,000 compared to $1,466,000 in fiscal 2005. Amortization of software costs, which was charged to cost of sales, was $1,224,000 and $988,000 for fiscal 2006 and fiscal 2005, respectively.

Impairment Expense.

Impairment expense resulted from the write-off of goodwill associated with our European subsidiary located in the United Kingdom. Although this subsidiary performs sales and service support for us, as of fiscal year end there were no open local contracts which would generate sufficient income to justify the carrying value of goodwill.

Operating Loss.

Operating loss was $4,719,000 compared to an operating loss of $7,130,000 in fiscal 2005, an improvement of $2,411,000 or 33.8%. This improvement primarily reflected reduced general and administrative spending partially offset by a reduced gross profit.

On a segment basis, TSG had an operating loss of $3,555,000, an improvement of $1,213,000 or 25.4% over fiscal 2005, while CSG had an operating loss of $362,000 in fiscal 2006, a reduction in operating loss of $1,156,000 from fiscal 2005. These segment operating results were offset, in part, by unallocated corporate expenses of $780,000, a decrease of $66,000 from fiscal 2005.

The decrease in operating loss for the TSG segment in fiscal 2006 reflected lower operating expenses, primarily claims and legal expenses, as both sales and corresponding gross profit were down from fiscal 2005.

The CSG segment's improved performance in fiscal 2006 reflected a higher gross margin despite the sales decrease coupled with slightly lower (down 9.8%) operating expenses.

Interest Expense.

Interest expense (net of interest income) increased $65,000 or 3.6% in fiscal 2006 from fiscal 2005 primarily reflecting additional deferred finance charges resulting from a settlement of a lawsuit which was partially offset by reduced interest expense on lower debt including the redemption on August 1, 2005, of our long-term bonds. Interest expense includes interest on our debt, amortization of debt discount resulting from the beneficial conversion option of our subordinated debt and associated warrants issued with the debt, amortization of deferred financing costs from our previous Refinancing, and amortization of debt discount resulting from the additional warrants issued to H.F. Lenfest in exchange for his guarantee on a portion of the bank facility in August 2004.

Bank Fees.

Bank fees decreased $308,000 or 76.8% in fiscal 2006 versus fiscal 2005 reflecting significantly reduced charges for bank agreement amendments and covenant violation waivers.

Letter of Credit Fees.

Letter of credit fees increased $39,000 or 76.5% in fiscal 2006 versus fiscal 2005 reflecting additional international contracts banking charges.

Other Income, net.

Other income, net, increased $55,000 or 38.5% in fiscal 2006 versus fiscal 2005 reflecting higher exchange gain in our Polish subsidiary, ETC-PZL.

Provision for/(Benefit from) Income Taxes.

Income tax expense in fiscal 2006 represented income taxes on pre-tax earnings in ETC-PZL and the establishment of a reserve for prior income tax benefits accrued on intercompany transactions losses. Although we reported a pre-tax consolidated operating loss during fiscal 2006, no offsetting income tax benefit and corresponding deferred tax asset was recorded, due to the uncertain nature of their ultimate realization based on past performance and the potential that sufficient taxable income may not be generated in the near future. We will recognize these benefits only as reassessment demonstrates that they are realizable. Realization is entirely dependent upon future earnings in specific tax jurisdictions.

The fiscal 2005 tax benefit reflects the realization of tax loss carry backs resulting from the fiscal 2005 loss. During fiscal 2006, we applied for and received refunds approximating $580,000.

Reflecting the Company's significant losses in the current and prior fiscal years, the Company has approximately $12.6 million of federal and $17.9 million of state net loss carry forwards available to offset future income tax liabilities, expiring in 2025. However, due to the uncertain nature of their ultimate realization based on past performance, and the potential that sufficient taxable income may not be generated in the near future, we have established a full valuation allowance of the same amount against these carry forward benefits and will recognize these benefits only as reassessment demonstrates that they are realizable. Realization is entirely dependent upon future earnings in specific tax jurisdictions. While the need for this valuation allowance is subject to periodic review, if the allowance is reduced, the tax benefits of the carry forwards will be recorded in future operations as a reduction of our income tax expense.

Liquidity and Capital Resources

During fiscal 2007, we used $6,997,000 of cash for operating activities. This cash was used to fund the operating loss, a build-up of inventories and a reduction in allowance for accounts receivable and inventories. These requirements for cash were partially offset by cash generation from non-cash expenses (depreciation and amortization of software and deferred finance charges), collections of accounts receivables and a reduction in costs and estimated earnings on uncompleted long-term contracts.

Our investing activities used $463,000 in fiscal 2007 and consisted of purchases of capital equipment ($308,000) and capitalized software ($155,000). Given the nature of our market and products, the continued development of generic control and core software and software tools is a critical objective of management.

Our financing activities generated $6,009,000 of cash during fiscal 2007. This primarily reflected the proceeds from the issuance of $6,000,000 of preferred stock.

Refinancing

We have historically financed operations through a combination of cash generated from operations, equity offerings, subordinated borrowings and bank debt. On February 19, 2003, we refinanced our operations (the "Refinancing"). The Refinancing was effected through the issuance of subordinated, convertible notes to H.F. Lenfest and a credit agreement (the "PNC Agreement") with PNC Bank, National Association ("PNC"). The total proceeds from this refinancing were $29,800,000.

Bank Credit and Facility

Since inception, the PNC Agreement has had numerous amendments. As of fiscal year end, the facility total was $5,000,000 and use of this amount was restricted to the issuance of international letters of credit. This line was secured by all of our assets as well as a $5,000,000 personal guarantee by Mr. Lenfest.

On November 16, 2006, we entered into a Letter Agreement with PNC Bank. This Letter Agreement amended, restated and replaced the existing PNC Credit Agreement. Pursuant to such agreement, PNC Bank (i) terminated our Credit Agreement dated as of February 18, 2003 (ii) re-approved our $5 million Line of Credit for Letters of Credit, and (iii) re-affirmed the Tangible Net Worth covenant (as defined in the Agreement) to a be a minimum of $9,000,000. The $5 million Line of Credit for Letters of Credit continued to be guaranteed by Mr. Lenfest. As of February 23, 2007, we had used approximately $2,607,000 of the availability under the PNC Agreement for international letters of credit.

Equity Line

On April 7, 2006, we entered into a Preferred Stock Purchase Agreement (the “Lenfest Equity Agreement”) with Mr. Lenfest. The Lenfest Equity Agreement, which terminates on October 6, 2007, permits us to unilaterally draw down up to $15 million in exchange for shares of our newly created Series B Cumulative Convertible Preferred Stock (“Preferred Stock”). The Preferred Stock provides for a dividend equal to six percent per annum. (To conserve cash outlay, Mr. Lenfest has agreed to defer the actual payment of all dividends until April 6, 2012, or upon 30 days written notice of demand.) After three years, the Preferred Stock will be convertible, at Mr. Lenfest’s request, into ETC common shares at a conversion price (the “Conversion Price”) which will be set on the day of each draw down. The Conversion Price will be equal to the closing price of our common stock on the trading day immediately preceding the day in which the draw down occurs, subject to a floor price of $4.95 per common share. Drawdowns will not be permitted on any day when the Conversion Price would be less than this floor price. On the sixth anniversary of the Lenfest Equity Agreement, any issued and outstanding Preferred Stock will be mandatorily converted into ETC common stock at each set Conversion Price. The Lenfest Equity Agreement also allows us to redeem any outstanding Preferred Stock any time within the six (6) year term of the Agreement. The Preferred Stock will vote with the ETC common stock on an as converted basis. In connection with the execution of the Lenfest Equity Agreement, the Company drew down $3 million by issuing 3,000 shares of Preferred Stock with a Conversion Price equal to $4.95 per share. Additionally, on July 31, 2006, we drew down an additional $3 million by issuing 3,000 shares of Preferred Stock at a conversion price equal to $6.68 per common share.

Unsecured Note

On November 16, 2006, we executed an Unsecured Promissory Note (the “Lenfest Note”) in favor of Mr. Lenfest in the aggregate principal amount of $3,000,000. Pursuant to the terms of the Lenfest Note, ETC can borrow up to $3,000,000, in increments of $1,000,000, prior to the maturity date of October 6, 2007. As of the date of this filing on Form 10-K, ETC had borrowed $2,000,000 under this line.

All outstanding and unpaid interest on the Lenfest Note is due and payable on the earlier of (i) October 6, 2007 or (ii) such date as ETC draws down funds sufficient to repay the amount due under the Lenfest Note pursuant to the Lenfest Equity Agreement.

Borrowings made pursuant to the Lenfest Note will bear interest at an annual rate of six percent with such interest beginning to accrue on the date of the funding of each loan and, to the extent not paid, compounding on the first day of each month.

The Lenfest Note provides for customary events of default including, but not limited to, the nonpayment of any amount payable when due, certain bankruptcy, insolvency or receivership events and the imposition of certain judgments. Upon the occurrence of an event of default, Mr. Lenfest has the right to accelerate the maturity date of the Lenfest Note and demand immediate payment of all amounts payable there under.

Subordinated Convertible Debt

In connection with the financing provided by PNC on February 19, 2003, we entered into a Convertible Note and Warrant Purchase Agreement with Mr. Lenfest (the “Subordinated Note”), pursuant to which we issued to Mr. Lenfest (i) a senior subordinated convertible promissory note in the original principal amount of $10,000,000 and (ii) warrants to purchase 803,048 shares of our common stock. Upon the occurrence of certain events, we will be obligated to issue additional warrants to Mr. Lenfest. The Subordinated Note accrues interest at the rate of 10% per annum (Mr. Lenfest reduced the rate to 8% on a temporary basis for the period December 1, 2004 through November 30, 2007) and matures on February 18, 2009. At our option, the quarterly interest payments may be deferred and added to the outstanding principal. (Starting with the payment which was due on December 1, 2006, Mr. Lenfest has agreed to defer payment of interest until February 18, 2009 or until such time as we receive written demand notice. He has also agreed to waive paying interest on deferred interest payments.) The Subordinated Note entitles Mr. Lenfest to convert all or a portion of the outstanding principal of, and accrued and unpaid interest on, the Subordinated Note into shares of common stock at a conversion price of $6.05 per share. The warrants may be exercised into shares of common stock at an exercise price equal to the lesser of $4.00 per share or two-thirds of the average of the high and low sale prices of the common stock for the 25 consecutive trading days immediately preceding the date of exercise.

Our obligations to Mr. Lenfest under the Subordinated note are secured by a second lien on all of our assets including all of our real property.

Prior to the consummation of the refinancing, Advanced Technology Asset Management, LLC (“ATAM”) (formerly ETC Asset Management, LLC), a shareholder and a holder of warrants to purchase 332,820 shares of our common stock, consented to the transactions contemplated under the Credit Agreement and the financing provided by Mr. Lenfest, including the below market issuance of warrants to Mr. Lenfest. As a result of its consent, ATAM waived, solely in connection with such issuance, the anti-dilution rights contained in its warrant. In exchange for ATAM’s consent, we issued to ATAM warrants to purchase an additional 105,000 shares of common stock. Except for the number of shares issuable upon exercise of the warrants, the new ATAM warrants have substantially the same terms as the warrants issued to Mr. Lenfest. In March 2004, ATAM exercised all its warrants and received a total of 437,820 shares of common stock. We received proceeds of $586,410 from the exercise of these warrants.

As a condition of amending the PNC Agreement on August 24, 2004, Mr. Lenfest agreed to issue to PNC on our behalf a limited guarantee to secure up to $5,000,000 in principal amount of any letters of credit issued under the amended facility. In consideration for issuing this guarantee, Mr.Lenfest will receive a fee of 0.75% per annum of the average amount of letters of credit

outstanding, payable on a quarterly basis, and received a warrant to purchase 200,000 shares of stock under the same terms and conditions as his warrant for 803,048 shares.

On February 14, 2005, Mr. Lenfest exercised all of his outstanding warrants and received 1,003,048 shares of common stock for approximately $3.9 million. Additionally, on February 14, 2005, Mr. Lenfest purchased 373,831 shares of common stock for approximately $2.0 million.

Under the Subordinated Note, we must meet certain financial covenants including a Leverage Ratio, a Fixed Charge Ratio and a Tangible Net Worth Ratio. At February 23, 2007 we failed to meet any of these financial covenants but have obtained a waiver from Mr. Lenfest. This waiver applies to the period through February 24, 2008. Except as specified, the waiver does not constitute a modification or alteration of any other terms or conditions in the Note, or a release of any of the lender's rights or remedies, all of which are reserved, nor does it release us or any guarantor from any duties, obligations, covenants or agreements including the consequences of any Event of Default, except as specified.

Long-Term Bonds

On March 15, 2000, we issued approximately $5,500,000 of unregistered Taxable Variable Rate Demand/Fixed Rate Revenue Bonds (Series of 2000). Net proceeds from these bonds were used to repay a $4,100,000 advance taken on our revolving credit facility and to finance construction of an addition to our main plant in Southampton, Pennsylvania. The bonds were secured by a $5,000,000 irrevocable direct pay Letter of Credit issued by PNC which was scheduled to expire on February 17, 2006 and which was secured by all assets of the Company. At February 25, 2005 the bonds were fully cash collateralized. The bonds carried a maturity date of April 1, 2020, bore a variable interest rate which adjusted each week to a rate required to remarket the bonds at full principal value with a cap of 17%, and were subject to mandatory redemption of $275,000 per year for 19 years and $245,000 for the 20th year.

On June 30, 2005 we directed the trustee for the bonds to issue a redemption notice for all of our outstanding bonds. On August 1, 2005, the Company utilized the restricted cash held by PNC to redeem all outstanding bonds. As of May 27, 2005, all deferred financing charges associated with this bond issue had been fully amortized to our statement of operations.

Lenfest Letter Agreement

Effective May 9, 2007, the Company entered into a letter agreement with H.F. Lenfest ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

Liquidity

Given our inability to borrow cash under the amended PNC Agreement and certain restrictions in the Lenfest Equity Agreement, we may need to obtain additional sources of capital in order to continue growing and operating our business. This capital may be difficult to obtain and the cost of this additional capital is likely to be relatively high. However, because we have established businesses in many markets, significant fixed assets including a building, and other valuable business assets which can be used for security, we believe that we will be able to locate such additional capital and that the actions by PNC will not have a long-term material adverse effect on our business.

Our ability to make debt payments depends on future performance, which, to a certain extent, is subject to general economic, financial, competitive and other factors, some of which are beyond our control. We are currently in negotiations with a bank to establish a line of credit which will either replace or supplant our existing equity line and unsecured note with Mr. Lenfest.

We believe that existing cash balances at February 23, 2007, cash generated from operating activities, future availability under either the Lenfest Equity Agreement, the Lenfest Note or the Letter Agreement with Mr. Lenfest and/or other arrangements with other lenders or investors will be adequate to meet our future obligations through at least March 1, 2008.

In reference to our outstanding claims with the U.S. Government, to the extent we are unsuccessful in recovering a significant portion of recorded claim contract costs, and to the extent that significant additional legal expenses are required to bring the dispute to resolution, such events could have a material adverse effect on our liquidity and results of operations. Historically, we have had a favorable experience in that recoveries have exceeded recorded claims, including significant settlement agreements in fiscal 2003, 2004 and 2005. (See Note 4 to the Consolidated Financial Statements, Accounts Receivable).

The following table presents our contractual cash flow commitments on long-term debt and operating leases. See Notes 8 and 9 to the Consolidated Financial Statements for additional information on our long-term debt and operating leases.

	Payments Due by Period (in thousands)				
	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
Long-term debt, including current maturities	$ 8,830	$ —	$ 8,830	$ —	$ —
Operating leases	616	129	394	93	—
Total	$ 9,446	$ 129	$ 9,224	$ 93	$ —

Long-term debt is reported net of unamortized discount of $1,170,000 on the Company's subordinated debt. See "Note 8. Long-Term Obligations and Credit Arrangements" to the Consolidated Financial Statements.

Backlog

Our sales backlog at February 23, 2007 and February 24, 2006, for work to be performed and revenue to be recognized under written agreements after such dates, was $13,564,000 and $8,132,000, respectively. In addition, our training, maintenance and upgrade contracts backlog at February 23, 2007 and February 24, 2006, for work to be performed and revenue to be recognized after such dates under written agreements, was $1,276,000 and $1,774,000, respectively. Of the February 23, 2007 backlog, approximately 68% was concentrated between environmental and aircrew training systems and maintenance support, including $4,945,000 for a domestic automotive customer and $1,568,000 for Indonesia.

We expect to complete approximately 88% of the February 23, 2007 backlog prior to February 29, 2008, the end of our 2008 fiscal year. Of the February 24, 2006 backlog, we completed approximately 75% by February 23, 2007.

Our order flow does not follow any seasonal pattern as we receive orders in each fiscal quarter of our fiscal year.

Off-Balance Sheet Arrangements

There were no off-balance sheet arrangements during the fiscal year ended February 23, 2007 that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to our investors.

Recent Accounting Pronouncements

Accounting for Share-Based Payments

In December 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123(R), Share-Based Payments. Statement No. 123(R) requires that the costs of employee share-based payments be measured at fair value on the awards' grant date using an option-pricing model and recognized in the financial statements over the requisite service period. Statement No. 123(R) does not change the accounting for stock ownership plans, which is subject to American Institute of Certified Public Accountants SOP 93-6, "Employer's Accounting for Employee Stock Ownership Plans." Statement No. 123(R) supercedes Opinion 25, Accounting for Stock Issued to Employees and its related interpretations, and eliminates the alternative to use Opinion 25's intrinsic value method of accounting, which we currently use.

Statement No. 123(R) allows for two alternative transition methods. The first method is the modified prospective application whereby compensation cost for the portion of awards for which the requisite service has not yet been rendered that are outstanding as of the adoption date will be recognized over the remaining service period. The compensation cost for that portion of awards will be based on the grant-date fair value of those awards as calculated for pro forma disclosures under Statement No. 123, as originally issued. All new awards and awards that are modified, repurchased, or cancelled after the adoption date will be accounted for under the provisions of Statement No. 123(R). The second method is the modified retrospective application, which requires that we restate prior period financial statements. The modified retrospective application may be applied either to all prior periods or only to prior interim periods in the year of adoption of Statement No. 123(R). We adopted Statement No. 123(R) effective February 25, 2006 utilizing the modified prospective application described above. Adoption of this statement did not have a significant impact on our financial position, results of operations, earnings per share or cash flows.

Accounting Changes and Error Corrections

In May 2005, the FASB issued FAS 154 *Accounting Changes and Error Corrections*. FAS 154, which supersedes Accounting Principles Bulletin (APB) 20, clarifies the accounting for accounting changes which includes:

- a change in accounting principle from one generally accepted accounting principle to another alternative that is considered preferable
- a change in an accounting estimate
- a change in the reporting entity

FAS 154 requires retrospective application of a newly adopted accounting principle, including changes in accounting principle required by newly issued pronouncements. It also requires the reporting of a change in depreciation, amortization, or depletion method as a change in an accounting estimate rather than a change in principle. It specifically restricts the use of the term "restatement" to the

correction of accounting errors (i.e., mathematical mistakes, mistakes in applying accounting principles, oversight or misuse of available facts, and use of unacceptable GAAP) in previously issued financial statements.

FAS 154 is effective for accounting changes and error corrections made in fiscal years beginning after December 15, 2005. The Company adopted Statement 154 effective with the first fiscal quarter of fiscal 2007 without any significant impact on the Company's consolidated financial position, results of operations or cash flow.

Accounting for Uncertainty in Income Taxes

In July 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes: an Interpretation of FASB Statement No. 109* ("FIN 48"*)*. FIN 48 clarifies Statement 109, *Accounting for Income Taxes*, to indicate a criterion that an individual tax position would have to meet for some or all of the benefit of that position to be recognized in an entity's financial statements. The Interpretation applies to all business enterprises including not-for-profit organizations. In applying FIN 48, an entity must evaluate a tax position, as defined, using a two-step process.

- evaluation for recognition: An entity should recognize the financial statement benefit of a tax position if it determines that it is more likely than not (i.e., a likelihood of more than 50 percent) that the position will be sustained on examination.
- measurement of the benefit: The amount recognized should be the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement.

FIN 48 also allows for subsequent recognition and derecognition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is not able at this time to determine what impact, if any, adoption of FIN 48 will have on the results of operations.

Accounting for Misstatements in Prior Year Financial Statements

In September 2006 the SEC issued Staff Accounting Bulletin 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 provides guidance on how prior year misstatements should be considered when quantifying misstatements in the current year financial statements. The SAB requires registrants to quantify misstatements using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 does not change the guidance in SAB 99, "Materiality", when evaluating the materiality of misstatements. SAB 108 is effective for fiscal years ended after November 15, 2006. Upon initial application, SAB 108 permits a one-time cumulative effect adjustment to beginning retained earnings. The Company adopted SAB 108 for fiscal 2007 and it had no material impact on consolidated financial statements.

Fair Value Measurements

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements, but does not require any new fair value measurements. SFAS No. 157 will become effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating what impact, if any, SFAS No. 157 will have on its financial condition, results of operations or liquidity.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 – *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159).which provides companies an option to report certain financial assets and liabilities at fair value. The intent of SFAS No. 159 is to reduce the complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS No. 159 is effective for financial statements issued for fiscal years after November 15, 2007. The Company is evaluating the impact this new standard will have on its financial position and results of operations.

Accounting for Inventory Costs

In November 2004, the FASB issued FASB Statement 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4. While retaining the general principle that inventories are presumed to be stated at cost, Statement 151 amends ARB No. 43 to clarify that:

- abnormal amounts of idle facilities, freight, handling costs, and spoilage should be recognized as charges of the current period.
- allocation of fixed production overheads to inventories should be based on the normal capacity of the production facilities.

Statement 151 defines normal capacity as the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance.

Statement 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005 and should be applied prospectively. Early application is permitted. The Company adopted SFAS No. 151 effective for its fiscal year ended February 23, 2007 without any significant impact on the Company's consolidated financial position, results of operations or cash flow.

Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	371,928	$ 6.70	1,198,882
Equity compensation plans not approved by security holders	—	N/A	203,837
Total	371,928	$ 6.70	1,402,719

The following plans have not been approved by our shareholders:

Employee Stock Purchase Plan

We have an Employee Stock Purchase Plan, which was adopted by the Board of Directors on November 3, 1987. All employees meeting service requirements, except officers, directors and 10% stockholders, are eligible to voluntarily purchase common stock through payroll deductions up to 10% of salary. We make a matching contribution equal to 20% of the employee's contribution.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
Environmental Tectonics Corporation

We have audited the accompanying consolidated balance sheets of Environmental Tectonics Corporation and Subsidiaries as of February 23, 2007 and February 24, 2006 and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for each of the three fiscal years in the period ended February 23, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Environmental Tectonics Corporation and Subsidiaries as of February 23, 2007 and February 24, 2006, and the consolidated results of their operations and their cash flows for the each of the three fiscal years in the period ended February 23, 2007 in conformity with accounting principles generally accepted in the United States of America.

We have also audited the accompanying Schedule II of Environmental Tectonics Corporation and Subsidiaries as of February 23, 2007 and February 24, 2006 and for each of the three fiscal years in the period ended February 24, 2006. In our opinion, this schedule presents fairly, in all material respects, the information required to be set forth herein.

Philadelphia, Pennsylvania
May 21, 2007

Environmental Tectonics Corporation
Consolidated Balance Sheets
(amounts in thousands, except share information)

	February 23, 2007	February 24, 2006
ASSETS		
Cash and cash equivalents	$ 2,215	$ 3,566
Restricted cash	20	16
Accounts receivable, net	5,098	6,021
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	2,816	3,480
Inventories	4,739	10,734
Deferred tax asset	1,262	1,558
Prepaid expenses and other current assets	213	564
Total current assets	16,363	25,939
Property, plant and equipment, net	4,054	4,392
Construction in progress	8,460	—
Software development costs, net of accumulated amortization of $10,949 and $9,882 in 2007 and 2006, respectively	2,158	2,832
Goodwill, net	455	455
Other assets, net	30	49
Total assets	$ 31,520	$ 33,667
LIABILITIES		
Accounts payable – trade	$ 2,254	$ 2,111
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	1,400	1,118
Customer deposits	794	877
Other accrued liabilities	2,207	2,013
Total current liabilities	6,655	6,119
Long-term obligations, less current portion:		
Subordinated convertible debt	8,830	8,376
Deferred tax liability	1,191	1,558
Total liabilities	16,676	16,053
Commitments and contingencies	—	—
Minority interest	53	61
STOCKHOLDERS' EQUITY		
Cumulative convertible preferred stock, $.05 par value, 15,000 shares authorized; 6,000 shares issued and outstanding at February 23, 2007	6,000	—
Common stock, $.05 par value, 20,000,000 shares authorized; 9,028,459 and 9,024,804 shares issued and outstanding at February 23, 2007 and February 23, 2006, respectively	451	451
Capital contributed in excess of par value of common stock	16,921	16,584
Accumulated other comprehensive loss	(149)	(249)
(Accumulated deficit) retained earnings	(8,432)	767
Total stockholders' equity	14,791	17,553
Total liabilities and stockholders' equity	$ 31,520	$ 33,667

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Consolidated Statements of Operations
(amounts in thousands, except share information)

	52 Weeks Ended February 23, 2007	52 Weeks Ended February 24, 2006	52 Weeks Ended February 25, 2005
Net sales	$ 17,419	$ 25,069	$ 27,814
Cost of goods sold	15,348	19,719	21,638
Gross profit	2,071	5,350	6,176
Operating expenses:			
Selling and administrative	9,434	9,625	12,450
Research and development	569	422	856
Impairment expense	—	22	—
	10,003	10,069	13,306
Operating loss	(7,932)	(4,719)	(7,130)
Other expenses:			
Interest expense, net	1,151	1,857	1,791
Bank fees	56	93	401
Letter of credit fees	70	90	51
Other, net	(184)	(198)	(143)
	1,093	1,842	2,100
Loss before provision for (benefit from) income taxes and minority interest	(9,025)	(6,561)	(9,230)
(Benefit from) provision for income taxes	(77)	136	(1,117)
Loss before minority interest	(8,948)	(6,697)	(8,113)
(Income) loss attributable to minority interest	8	(17)	—
Net loss	$ (8,940)	$ (6,714)	$ (8,113)
Per share information:			
Loss per common share:			
Basic	$ (1.02)	$ (0.74)	$ (1.06)
Diluted	$ (1.02)	$ (0.74)	$ (1.06)
Weighted average common shares:			
Basic	9,030,000	9,021,000	7,656,000
Diluted	9,030,000	9,021,000	7,656,000

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Consolidated Statements of Changes in Stockholders' Equity
(amounts in thousands, except share information)

For the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005

	Preferred Stock	Common Stock Shares	Common Stock Amount	Capital contributed in excess of par value of common stock	Accumulated other comprehensive loss	Retained earnings (deficit)	Total stockholders' equity
Balance, February 27, 2004		**7,176,552**	**359**	**9,430**	**(329)**	**15,594**	**25,054**
Net loss for the year	—	—	—	—	—	(8,113)	(8,113)
Foreign currency translation adjustment					192	—	192
Total comprehensive loss							(7,921)
Value of warrants issued in connection with issuance of guarantee				571			571
Exercise of warrants		1,440,868	72	4,406			4,478
Issuance of common stock		373,831	19	1,981			2,000
Exercise of employee stock options and Board of Director's compensation	—	28,125	—	173	—	—	173
Balance, February 25, 2005	**—**	**9,019,376**	**450**	**16,561**	**(137)**	**7,481**	**24,355**
Net loss for the year						(6,714)	(6,714)
Foreign currency translation adjustment					(112)		(112)
Total comprehensive loss							(6,826)
Exercise of employee stock options and Board of Director's compensation	—	5,428	1	23	—	—	24
Balance, February 24, 2006	—	9,024,804	451	16,584	(249)	767	17,553
Net loss for the year						(8,940)	(8,940)
Foreign currency translation adjustment					100		100
Total comprehensive loss							(8,840)
Stock option expense				324			324
Exercise of employee stock options and Board of Director's compensation		3,655	—	13	—	—	13
Issuance of preferred stock	6,000	—	—	—	—	—	6,000
Dividend payable on preferred stock	—	—	—	—	—	(259)	(259)
Balance, February 23, 2007	**6,000**	**9,028,459**	**$ 451**	**$ 16,921**	**$ (149)**	**$ (8,432)**	**$ 14,791**

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Consolidated Statements of Cash Flows
(amounts in thousands)

	52 Weeks Ended February 23, 2007	52 Weeks Ended February 24, 2006	52 Weeks Ended February 25, 2005
Cash flows from operating activities:			
Net loss	$ (8,940)	$ (6,714)	$ (8,113)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities			
Depreciation and amortization	1,857	2,570	2,414
Accretion of debt discount	454	384	326
(Decrease) increase in allowance for accounts receivable and inventory	(638)	780	274
(Income) loss attributable to minority interest	(8)	17	—
Impairment expense	—	22	—
Stock option compensation expense	324	—	—
Deferred income taxes (benefit)	(71)	—	(165)
Changes in operating assets and liabilities:			
(Increase) decrease in assets:			
Accounts receivable	1,520	1,518	11,108
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	664	(147)	2,000
Inventories	(2,806)	(3,468)	1,554
Prepaid expenses and other current assets	351	480	318
Other assets	19	(26)	—
Increase (decrease) in liabilities:			
Accounts payable	143	(782)	462
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	282	(415)	588
Customer deposits	(83)	(1,370)	(1,410)
Accrued income taxes	43	76	266
Other accrued liabilities	(108)	(774)	101
Net cash (used in) provided by operating activities	(6,997)	(7,849)	9,723
Cash flows from investing activities:			
Acquisition of equipment	(308)	(343)	(285)
Software development costs	(155)	(489)	(1,272)
Net cash used in investing activities	(463)	(832)	(1,557)
Cash flows from financing activities:			
Borrowings under credit facility	3,000	—	—
Payments under credit facility	(3,000)	—	(30)
Payments on long-term bonds	—	(4,370)	(275)
Issuance of preferred stock	6,000	—	—
(Increase) decrease in restricted cash	(4)	4,664	(3,896)
Net decrease in other long-term obligations	—	—	(133)
Issuance of common stock/warrants	13	24	6,651
Net cash provided by financing activities	6,009	318	2,317
Effect of exchange rates on cash	100	(112)	192
Net (decrease) increase in cash and cash equivalents	(1,351)	(8,475)	10,675
Cash and cash equivalents at beginning of year	3,566	12,041	1,366
Cash and cash equivalents at end of year	$ 2,215	$ 3,566	$ 12,041
Supplemental schedule of cash flow information:			
Interest paid	$ 616	$ 886	$ 909
Income taxes paid	$ —	$ —	$ 5

Supplemental information on non-cash operating, investing and financing activities:

In the year ended February 23, 2007, the Company reclassified $8,460,000 from inventory to construction in progress. During the years ended February 23, 2007, and February 25, 2005, the Company reclassified $382,000 and $194,000, respectively, from inventory to capitalized software. During the year ended February 24, 2006 the Company reclassified $361,000 from inventory to property, plant and equipment. Additionally, during the year ended February 25, 2005, the Company recorded $571,000 in deferred finance charges and credited a corresponding amount to additional paid in capital associated

with the issuance of a common stock purchase warrant to H.F. Lenfest. As of February 23, 2007, this amount had been fully amortized to operations.

The accompanying notes are an integral part of the consolidated financial statements.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements

1. Nature of Business and Liquidity Matters:

Environmental Tectonics Corporation ("ETC" or the "Company") is principally engaged in the design, manufacture and sale of software driven products and services used to recreate and monitor the physiological effects of motion on humans and equipment and to control, modify, simulate and measure environmental conditions. These products include aircrew training systems (aeromedical, tactical combat and general), disaster management systems and services, entertainment products, sterilizers (steam and gas), environmental testing products and hyperbaric chambers and other products that involve similar manufacturing techniques and engineering technologies. ETC focuses on software enhancements, product extensions, new product development and new marketplace applications. Sales of its products are made principally to U.S. and foreign government agencies and to the entertainment market. We operate in two primary business segments, the Training Services Group (TSG) (formerly Aircrew Training Systems (ATS)) and the Control Systems Group (CSG) (formerly the Industrial Group (IG)).

Training Services Group. This segment includes three primary product groups: aircrew training devices and services, disaster management training and systems, and entertainment products.

Control Systems Group. This segment includes three primary product lines: sterilizers, environmental control systems and other products, and hyperbarics.

The Company has experienced net cash usages from operations of $6,997,000 and $7,849,000 for fiscal years 2007 and 2006, respectively. The Company does not currently have a bank facility which can be used to borrow funds for operating purposes. The Company's Letter Agreement with PNC Bank, which is restricted to use for letters of credit, expires in June 2007. In addition to cash from collections, the Company's has two sources of cash, the Lenfest Equity Line and the Lenfest Note, both of which expire in October 2007 (See Note 8. Long-Term Obligations and Credit Arrangements).

2. Subsequent Event:

Effective May 9, 2007, the Company entered into a letter agreement with H.F. Lenfest, a Company director, ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

3. Summary of Significant Accounting Policies:

Principles of Consolidation:

The consolidated financial statements include the accounts of Environmental Tectonics Corporation, its wholly owned subsidiaries Entertainment Technology Corporation, ETC Delaware, and ETC International Corporation, its 95% owned subsidiary, ETC-PZL Aerospace Industries SP. Z 0.0, and its 99% owned subsidiary, ETC Europe. All material inter-company accounts and transactions have been eliminated in consolidation. The Company's fiscal year is the 52-or 53-week annual accounting period ending the last Friday in February.

Use of Estimates:

In preparing financial statements in conformity with accounting principles generally accepted in the United States, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are made for revenue recognition under the percentage of completion method, claims receivable, inventories and computer software costs.

Total claims outstanding at February 23, 2007 were approximately $8.0 million based on costs incurred through April 2005. However, following generally accepted accounting principles, the Company had recorded only $3.0 million or 37.5% of this amount on its books.

Significant claims outstanding at February 23, 2007 and February 25, 2006 included a claim with the U.S. Navy for a submarine decompression chamber ($3.0 million recorded). Significant claims outstanding at February 27, 2004 included $2.9 million for the aforementioned U.S. Navy claim and $2.6 million for an international customer. Effective February 27, 2004 the Company reached an agreement totaling $10.5 million on a prior international claim. This settlement was paid to the Company in March 2004. On

February 8, 2005, the Company reached an agreement totaling $4.7 million on the remaining international claim. This settlement was paid to the Company in February 2005.

Although recorded as a current asset in the financial statements, all remaining claim revenues may not be received in full during fiscal 2008. For a more complete discussion of outstanding claims, see "Note 4. Accounts Receivable" to our consolidated financial statements in the Annual Report to Stockholders following.

Revenue Recognition:

Revenue is recognized on long-term contracts over $250,000 in value and six months in length utilizing the percentage of completion method based on costs incurred as a percentage of estimated total costs. Revenue recognized on uncompleted long-term contracts in excess of amounts billed to customers is reflected as a current asset. Amounts billed to customers in excess of revenue recognized on uncompleted long-term contracts are reflected as a current liability. When it is estimated that a contract will result in a loss, the entire amount of the estimated loss is accrued. The effect of revisions in cost and profit estimates for long-term contracts is reflected in the accounting period in which the facts requiring the revisions become known. Contract progress billings are based upon contract provisions for customer advance payments, contract costs incurred and completion of specified contract milestones. Contracts may provide for customer retainage of a portion of amounts billed until contract completion. Retainage is generally due within one year of completion of the contract. Revenue for contracts under $250,000 or to be completed in less than six months, and where there are no post-shipment services included in the contract, and revenue on parts and services, are recognized as shipped or when the service is provided. Under these contracts, title passes at shipment. Revenue on those types of contracts where post-shipment services (such as installation and acceptance) are required is recognized upon customer acceptance. Revenue for service contracts is recognized ratably over the life of the contract with related material costs expensed as incurred.

Cash and Cash Equivalents:

Cash and cash equivalents include short-term deposits at market interest rates with original maturities of three months or less. The Company maintains cash balances at several financial institutions located in the Northeast United States and at some locations internationally. Accounts in each domestic institution are insured by the Federal Deposit Insurance Corporation up to $100,000. During each fiscal year, the Company periodically has cash and cash equivalents in excess of insured amounts. However, significant portions of the Company's funds are with one financial institution, which has had no experience of significant customer losses to date.

Restricted Cash:

Restricted cash represents a restricted cash deposit in a local bank.

Inventories:

Inventories are valued at the lower of cost or market. Cost is determined principally by the first-in, first-out method. The costs of finished goods and work-in-process inventories include material, direct engineering, manufacturing labor and overhead components. The Company periodically reviews the net realizable value of the inventory and, if necessary, writes down the recorded costs.

Depreciation of Property, Plant and Equipment:

Property, plant and equipment are depreciated over their estimated useful lives by the straight-line method for financial reporting purposes. Accelerated depreciation methods are used for tax purposes. Upon sale or retirement of property, plant and equipment, the costs and related accumulated depreciation are eliminated from the accounts. Any resulting gains or losses are included in the determination of net income.

Goodwill:

Goodwill of $662,000 was recorded in fiscal 1999 for the Company's 65% ownership purchase of ETC-PZL Aerospace Industries, SP. Z O.O. On September 27, 2000, the Company purchased an additional 30% ownership for $300,000 cash, bringing the Company's total ownership to 95%. Goodwill of $24,000 was recorded in fiscal 2001 for the Company's purchase of 99% of ETC Europe. The Company did not record any amortization expense in fiscal years 2007, 2006 and 2005, respectively. Based on a test of impairment, the Company did not reduce the net carrying values of goodwill for the purchase of ETC-PZL for fiscal years 2007 and 2006. However, based upon the impairment test at February 24, 2006, the Company charged off to the operating statement the remaining $22,000 of goodwill associated with the purchase of ETC Europe.

The following summarizes the goodwill and associated amortization of the elements of goodwill at February 23, 2007:

(Amounts in thousands)	
Goodwill	$ 662
Amortization	(207)
Net	$ 455

On February 23, 2002, we adopted Statement of Financial Accounting Standards No. 142 “Goodwill and Intangible Assets”. SFAS No. 142 includes requirements to annually test goodwill and indefinite lived intangible assets for impairment rather than amortize them. Accordingly, we no longer amortize goodwill.

Capitalized Software Development Costs:

The Company capitalizes the qualifying costs of developing software contained in certain products. Capitalization of costs requires that technological feasibility has been established. When the software is fully documented and tested, capitalization of development costs cease and amortization commences on a straight-line basis over a period ranging from 36 to 60 months, depending upon the life of the product, which, at a minimum, approximates estimated sales. Realization of capitalized software costs is subject to the Company’s ability to market the related product in the future and generate cash flows to support future operations. Capitalized software costs totaled $537,000 and $489,000 respectively, for the fiscal years ended February 23, 2007 and February 24, 2006. Related software amortization totaled $1,231,000 **,** $1,224,000 and $988,000, respectively, for fiscal 2007, 2006 and 2005.

Research and Development:

Research and development expenses are charged to operations as incurred. During fiscal 2007, 2006 and 2005, the Company incurred research and development costs of approximately $569,000, $422,000 and $856,000, respectively.

Deferred Financing Costs:

Capitalized costs relating to the Company’s bond issuance on March 15, 2000, costs associated with the February 2003 PNC/Lenfest financing and costs associated with the issuance in fiscal 2005 of a common stock warrant have been amortized over the relevant term. Amortization expense relating to deferred financing costs was $703,000 and $587,000 in fiscal 2006 and 2005, respectively. At February 23, 2007, the Company had no deferred financing costs.

See “Note 8. Long-Term Obligations and Credit Arrangements” to the Consolidated Financial Statements.

Income Taxes:

The Company accounts for income taxes using the liability method, which reflects the impact of temporary differences between values recorded for assets and liabilities for financial reporting purposes and values utilized for measurement in accordance with applicable tax laws.

Long-Lived Assets:

In accordance with SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets”, the Company periodically evaluates the period of depreciation or amortization for long-lived assets to determine whether current circumstances warrant revised estimates of useful lives. The Company reviews its property and equipment for impairment whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. Recoverability is measured by a comparison of the carrying amount to the net undiscounted cash flows expected to be generated by the asset. An impairment loss would be recorded for the excess of net book value over the fair value of the asset impaired. The fair value is estimated based on expected discounted future cash flows.

The results of impairment tests are subject to management’s estimates and assumptions of projected cash flows and operating results.

Share-Based Compensation:

The Company adopted Statement of Financial Accounting Standard (“SFAS”) No. 123(R) effective February 25, 2006. SFAS No. 123(R) requires the Company to recognize expense related to the fair value of stock-based compensation awards, including employee stock options. Prior to the adoption of SFAS No. 123(R), the Company accounted for stock options using the intrinsic value method of APB Opinion No. 25, and it did not recognize compensation expense in its income statement for options granted that had an

exercise price equal to the market value of the underlying common stock on the date of grant. The Company also provided certain pro forma disclosures for stock option awards as if the fair value-based approach of SFAS No. 123(R) had been applied.

The Company has elected to use the modified prospective transition method as permitted by SFAS No. 123(R) and therefore has not restated its financial results for prior periods. Under this transition method, the Company will apply the provisions of SFAS No. 123(R) to new awards and to awards modified, repurchased or cancelled after February 24, 2006. Additionally, for unvested awards granted prior to the effective date of the Company's adoption of SFAS No. 123(R), the Company recognizes compensation expense in the same manner as was used in its income statement or for pro-forma disclosures prior to the effective date of its adoption of SFAS No. 123(R).

The cost for stock option compensation was $324,000 for the year ended February 23, 2007.

As February 23, 2007, the remaining prospective pre-tax cost of unvested stock option employee compensation was $158,000, which will be expensed on a pro-rata basis going forward.

At February 23, 2007, the Company had two stock-based compensation plans, one for employees and one for non-employee members of the Board of Directors.

Employee Stock Plan:

In August 1999, the Company adopted an Incentive Stock Option Plan to replace the 1988 Incentive Stock Option Plan which expired in August 1999. The plan authorizes a committee of the Board of Directors to grant options for the purchase of up to 1,000,000 shares of common stock to qualifying officers and other key employees. The plan provides that option price shall not be less than 100% (or in the case of a ten percent owner, 110%) of the current market price of the stock on the date of the grant. Depending on specific grants, options may be exercised on a cumulative basis at the rate of either 50% or 25% per year commencing one year after the date of grant and have a maximum term of 10 years. The Plan will terminate on August 1, 2008. At February 23, 2007, there were 678,882 shares available to be granted under the Plan.

Non-employee Director Stock Plan:

In September 2005, the Company adopted subsequent to shareholder approval a stock option plan which allows for the granting to non-employee members of ETC's Board of Directors of options to purchase up to 600,000 shares of common stock. The plan provides that option price shall not be less than 100% of the current market price of the stock on the date of the grant. The amount of each individual award and the vesting period are determined by the Board of Directors or its appointed committee. Granted options have a maximum term of 10 years. The Plan shall remain in effect until terminated by the Board of Directors. At February 23, 2007, there were 520,000 shares available to be granted under the Plan.

The following table illustrates the effect on net loss and net loss per common share as if the Company had applied the fair value recognition provisions of SFAS No. 123(R) to stock option employee compensation for the years ended February 24, 2006 and February 25, 2005:

(amounts in thousands)

	52 Weeks Ended February 24, 2006	52 Weeks Ended February 25, 2005
Net loss, as reported	$ (6,714)	$ (8,113)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(91)	(30)
Pro forma net loss	$ (6,805)	$ (8,143)
Loss per share:		
Basic—as reported	$ (0.74)	$ (1.06)
Basic—pro forma	$ (0.75)	$ (1.06)
Diluted—as reported	$ (0.74)	$ (1.06)
Diluted—pro forma	$ (0.75)	$ (1.06)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted average assumptions used for grants in fiscal 2007: expected volatility of 45.4% to 53.4%; risk-free interest rate of 4.56% and 4.71%; and an expected life of 10 years. The weighted average assumptions used for grants in fiscal 2005 were as follows: expected volatility of 30.2%; risk-free interest rate of 4.14%; and an expected life of 10 years. There were no grants in fiscal 2006.

Advertising Costs:

The Company expenses advertising costs, which include trade shows, as incurred. Advertising expense was $351,000, $302,000 and $310,000 in fiscal 2007, 2006, and 2005, respectively.

Earnings Per Common Share:

SFAS No. 128, “Earnings Per Share”, requires presentation of basic and diluted earnings per share together with disclosure describing the computation of the per share amounts. Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

The following table illustrates the reconciliations of the numerators and denominators of the basic and diluted earnings per share computations.

(amounts in thousands)

	Fiscal years ended: February 23, 2007	February 24, 2006	February 25, 2005
Net loss	$ (8,940)	$ (6,714)	$ (8,113)
Preferred stock dividend	(259)	—	—
Loss applicable to common stockholders	$ (9,199)	$ (6,714)	$ (8,113)
Weighted average shares	9,030,000	9,021,000	7,656,000
Basic loss per common share	$ (1.02)	$ (0.74)	$ (1.06)
Dilutive loss per common share:			
Effect of dilutive securities:			
Stock options (A)	—	—	—
Convertible debt (B)	—	—	—
Preferred stock (C)	—	na	na
Dilutive loss per common share:	$ (1.02)	$ (0.74)	$ (1.06)

Potentially dilutive common shares, which were not included in the computation of diluted loss per share, included the following:

A. Outstanding options to purchase the Company’s common stock totaling 371,928, 327,939 and 276,162 shares as of February 23, 2007, February 24, 2006 and February 25, 2005, respectively.

B. Convertible subordinated debt, with a face value of $10,000,000, which is convertible into shares of common stock at an exercise price of $6.05 per share, equating to 1,652,893 shares of common stock if fully converted. Upon each conversion of the subordinated note, the holder will be entitled to receive a warrant to purchase additional shares of common stock equal to ten percent of the shares issued pursuant to such conversion. If the entire face value of the subordinated note were to be converted into shares of common stock, then warrants to purchase an additional 165,289 shares of common stock would be issued, bringing the total number of shares of common stock to be issued to 1,818,182.

C. Convertible preferred stock issued in fiscal 2007 totaling $6,000,000 which is convertible into 1,055,161 shares of common stock. The conversion price for $3,000,000 of the preferred stock is $4.95 per common share and the remaining $3,000,000 is convertible at $6.68 per common share. The net loss in fiscal 2007 was adjusted by the aggregate amounts of dividends on the preferred stock.

None of these shares were included in the computation of diluted loss per share as the effect would be anti-dilutive.

Recent Accounting Pronouncements

Accounting for Share-Based Payments

In December 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123(R), Share-Based Payments. Statement No. 123(R) requires that the costs of employee share-based payments be measured at fair value on the awards' grant date using an option-pricing model and recognized in the financial statements over the requisite service period. Statement No. 123(R) does not change the accounting for stock ownership plans, which is subject to American Institute of Certified Public Accountants SOP 93-6, "Employer's Accounting for Employee Stock Ownership Plans." Statement No. 123(R) supercedes Opinion 25, Accounting for Stock Issued to Employees and its related interpretations, and eliminates the alternative to use Opinion 25's intrinsic value method of accounting, which we currently use.

Statement No. 123(R) allows for two alternative transition methods. The first method is the modified prospective application whereby compensation cost for the portion of awards for which the requisite service has not yet been rendered that are outstanding as of the adoption date will be recognized over the remaining service period. The compensation cost for that portion of awards will be based on the grant-date fair value of those awards as calculated for pro forma disclosures under Statement No. 123, as originally issued. All new awards and awards that are modified, repurchased, or cancelled after the adoption date will be accounted for under the provisions of Statement No. 123(R). The second method is the modified retrospective application, which requires that we restate prior period financial statements. The modified retrospective application may be applied either to all prior periods or only to prior interim periods in the year of adoption of Statement No. 123(R). We adopted Statement No. 123(R) effective February 25, 2006 utilizing the modified prospective application described above. Adoption of this statement did not have a significant impact on our financial position, results of operations, earnings per share or cash flows.

Accounting Changes and Error Corrections

In May 2005, the FASB issued FAS 154 *Accounting Changes and Error Corrections*. FAS 154, which supersedes Accounting Principles Bulletin (APB) 20, clarifies the accounting for accounting changes which includes:

- a change in accounting principle from one generally accepted accounting principle to another alternative that is considered preferable
- a change in an accounting estimate
- a change in the reporting entity

FAS 154 requires retrospective application of a newly adopted accounting principle, including changes in accounting principle required by newly issued pronouncements. It also requires the reporting of a change in depreciation, amortization, or depletion method as a change in an accounting estimate rather than a change in principle. It specifically restricts the use of the term "restatement" to the correction of accounting errors (i.e., mathematical mistakes, mistakes in applying accounting principles, oversight or misuse of available facts, and use of unacceptable GAAP) in previously issued financial statements.

FAS 154 is effective for accounting changes and error corrections made in fiscal years beginning after December 15, 2005. The Company adopted Statement 154 effective with the first fiscal quarter of fiscal 2007 without any significant impact on the Company's consolidated financial position, results of operations or cash flow.

Accounting for Uncertainty in Income Taxes

In July 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes: an Interpretation of FASB Statement No. 109* ("FIN 48"*)*. FIN 48 clarifies Statement 109, *Accounting for Income Taxes*, to indicate a criterion that an individual tax position would have to meet for some or all of the benefit of that position to be recognized in an entity's financial statements. The Interpretation applies to all business enterprises including not-for-profit organizations. In applying FIN 48, an entity must evaluate a tax position, as defined, using a two-step process.

- evaluation for recognition: An entity should recognize the financial statement benefit of a tax position if it determines that it is more likely than not (i.e., a likelihood of more than 50 percent) that the position will be sustained on examination.
- measurement of the benefit: The amount recognized should be the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement.

FIN 48 also allows for subsequent recognition and derecognition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is not able at this time to determine what impact, if any, adoption of FIN 48 will have on the results of operations.

Accounting for Misstatements in Prior Year Financial Statements

In September 2006 the SEC issued Staff Accounting Bulletin 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 provides guidance on how prior year misstatements should be considered when quantifying misstatements in the current year financial statements. The SAB requires registrants to quantify misstatements using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 does not change the guidance in SAB 99, "Materiality", when evaluating the materiality of misstatements. SAB 108 is effective for fiscal years ended after November 15, 2006. Upon initial application, SAB 108 permits a one-time cumulative effect adjustment to beginning retained earnings. The Company adopted SAB 108 for fiscal 2007 and it had no material impact on consolidated financial statements.

Fair Value Measurements

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements, but does not require any new fair value measurements. SFAS No. 157 will become effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating what impact, if any, SFAS No. 157 will have on its financial condition, results of operations or liquidity.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 – *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159).which provides companies an option to report certain financial assets and liabilities at fair value. The intent of SFAS No. 159 is to reduce the complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS No. 159 is effective for financial statements issued for fiscal years after November 15, 2007. The Company is evaluating the impact this new standard will have on its financial position and results of operations.

Accounting for Inventory Costs

In November 2004, the FASB issued FASB Statement 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4. While retaining the general principle that inventories are presumed to be stated at cost, Statement 151 amends ARB No. 43 to clarify that:

- abnormal amounts of idle facilities, freight, handling costs, and spoilage should be recognized as charges of the current period.
- allocation of fixed production overheads to inventories should be based on the normal capacity of the production facilities.

Statement 151 defines normal capacity as the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance.

Statement 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005 and should be applied prospectively. Early application is permitted. The Company adopted SFAS No. 151 effective for its fiscal year ended February 23, 2007 without any significant impact on the Company's consolidated financial position, results of operations or cash flow.

4. Accounts Receivable:

The components of accounts receivable at February 23, 2007 and February 24, 2006 are as follows:

	(amounts in thousands)	
	2007	2006
U.S. government receivables billed and unbilled contract costs subject to negotiation	$ 3,135	$ 3,346
U.S. commercial receivables billed	1,525	2,297
International receivables billed	806	1,343
	5,466	6,986
Less allowance for doubtful accounts	(368)	(965)
	$ 5,098	$ 6,021

U.S. government receivables billed and unbilled contract costs subject to negotiation:

Unbilled contract costs subject to negotiation as of February 23, 2007, represent claims made against the U.S. Government under a contract for a submarine rescue decompression chamber project. These costs totaling $3,004,000 were recorded beginning in fiscal year 2002 and include $375,000 recorded in fiscal 2002, $1,691,000 recorded during fiscal 2003, $833,000 recorded during fiscal year 2004 and $105,000 recorded during fiscal year 2005. In November 2003, the U.S. Government completed an audit of the claim, rejecting most of the items due to audit or engineering reasons. The Company has submitted a written rebuttal to the draft report. On July 22, 2004, the U.S. Government's Contracting Officer issued a final decision on the claim, denying the claim in full. The Company has updated the claim for additional costs expended on claimable items since the original submission and has converted the claim to a complaint, which was filed in the Court of Federal Claims in July 2005. This claim is currently scheduled for trial in July 2007.

This U. S. Government claim has followed the typical process of claim notification, preparation, submittal, government audit and review by the contracting officer. However, this claim was filed in the Court of Federal Appeals whereas prior government claims were filed with the Armed Services Board of Contract Appeals (ASBCA), which has complicated the litigation process. Historically, the Company's experience has been that most claims are initially denied in part or in full by the contracting officer (or no decision is forthcoming, which is then taken to be a deemed denial) which then forces the Company to seek relief in a court of law.

The Company considers the recorded costs to be realizable due to the fact that the costs relate to customer caused delays, errors and changes in specifications and designs, disputed liquidated damages and other out of scope items. In the first quarter of fiscal 2005, the Company submitted a supplement to the claim incorporating additional cost items. The U.S. Government, citing failure to deliver the product within contract terms, has assessed liquidated damages but has not offset or withheld any progress payments due to the Company under the contract. The Company disputes the basis for these liquidated damages, noting that applicable U.S. Government purchasing regulations allow for a waiver of these charges if the delay is beyond the control and not due to the fault or negligence of the Company. However, following accounting principles generally accepted in the United States of America, the Company has reduced contract values and corresponding revenue recognition for an estimated amount of $330,000 to cover a delay through the extended delivery period.

International receivables billed:

International receivables billed include $700,000 at February 23, 2007 and February 24, 2006, respectively, related to a contract with the Royal Thai Air Force ("RTAF").

In October 1993, the Company was notified by the RTAF that the RTAF was terminating a $4,600,000 simulator contract with the Company. Although the Company had performed in excess of 90% of the contract, the RTAF alleged a failure to completely perform. In connection with this termination, the RTAF made a call on a $230,000 performance bond, as well as a draw on an approximately $1,100,000 advance payment letter of credit. Work under this contract had stopped while under arbitration, but on October 1, 1996, the Thai Trade Arbitration Counsel rendered its decision under which the contract was reinstated in full and the Company was given a period of nine months to complete the remainder of the work. Except as noted in the award, the rights and obligations of the parties remained as stated in the original contract including the potential invoking of penalties or termination of the contract for delay. On December 22, 1997, the Company successfully performed acceptance testing and the unit passed with no discrepancy reports. Although the contract was not completed in the time allotted, the Company had requested an extension on the completion time due to various extenuating circumstances, including allowable "force majeure" events, one of which was a delay in obtaining an export license to ship parts required to complete the trainers. On August 30, 2001, the Company received a payment of $230,000 representing the amount due on the performance bond.

The open balance of $700,000 due on the contract represents the total gross exposure to the Company on this contract. On June 16, 2003, the Company filed for arbitration in Thailand seeking recovery of the $700,000 open balance on this contract. On March 23, 2006, the arbitration panel awarded the Company $314,813 plus interest from March 1, 2006 as full settlement of this dispute. Although this award is final with the arbitration panel, the RTAF has filed a motion in the Thai court to void the award, citing that the award was illegal and thus against the public order and unfair to the RTAF. On August 9, 2006, the Company filed its defense to this motion with the court. In September 2006, at a pre-trial session the court ordered the parties to produce witnesses to testify. This testimony has been scheduled for August and September 2007.

If the RTAF loses on its motion but does not honor the decision, the award will have to be enforced through the court system in Thailand, a process which may be time consuming and costly. The assets of the RTAF are not subject to attachment. At this point, the Company is not able to determine the ultimate outcome of this dispute. However, the Company has established sufficient receivable reserves so that any resolution will not have a material impact on the Company's financial position or its results of operations.

Historically, the Company has had positive experience with regard to its contract claims in that recoveries have exceeded the carrying value of claims. However, there is no assurance that the Company will always have positive experience with regard to recoveries for its contract claims.

Claim bookings and settlements had no impact in fiscal 2007 and 2006; in fiscal 2005 they reduced operating income by $1,124,000.

Net claims receivables were $3,004,000 at February 23, 2007 and February 24, 2006.

5. Costs and Estimated Earnings on Uncompleted Contracts:

Unbilled costs

Amounts not billed or not yet billable totaled $12,314,000 at February 23, 2007. Under most of the Company's contracts, invoices are issued upon the attainment of certain contract milestones, for example upon receipt of order, upon engineering drawing submittal, upon design acceptance, or upon shipment. Service contracts are billed monthly or quarterly. Parts and service are billed as shipped or completed.

The following is a summary of long-term contracts in progress at February 23, 2007 and February 24, 2006:

	(amounts in thousands)	
	2007	2006
Costs incurred on uncompleted long-term contracts	$ 40,395	$ 37,608
Estimated earnings	14,954	7,744
	55,348	45,352
Less billings to date	(53,932)	(42,990)
	$ 1,416	$ 2,362

	2007	2006
Included in accompanying balance sheets under the following captions:		
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	$ 2,816	$ 3,480
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	(1,400)	(1,118)
	$ 1,416	$ 2,362

Included in billings in excess of costs and estimated earnings on uncompleted long-term contracts is a provision for anticipated losses on contracts of $200,000 in fiscal 2007, 2006 and 2005.

6. Inventories:

Inventories consist of the following:

	(amounts in thousands)			
	Raw Material	Work in Process	Finished Goods	Total
February 23, 2007	$ 95	$3,820	$ 824	$ 4,739
February 24, 2006	$ 158	$8,803	$ 1,773	$10,734

Inventory is presented above net of an allowance for obsolescence of $991,000 and $1,032,000 in fiscal 2007 and 2006, respectively.

7. Property, Plant and Equipment:

The following is a summary of property, plant and equipment, at cost, and estimated useful lives at February 23, 2007 and February 24, 2006:

	(amounts in thousands) 2007	2006	Estimated useful lives
Land	$ 100	$ 100	
Building and building additions	3,763	3,763	40 years
Machinery and equipment	10,024	10,008	3-5 years
Office furniture and equipment	1,379	1,195	10 years
Building improvements	1,548	1,460	5-10 years
	16,814	16,526	
Less accumulated depreciation	(12,760)	(12,134)	
Property, plant and equipment, net	$ 4,054	$ 4,392	

Depreciation expense for the fiscal years ended February 23, 2007, February 24, 2006 and February 25, 2005 was $624,000, $643,000 and $840,000, respectively. The Company has recorded as Construction in Progress $8,460,000 in costs for building improvements and equipment associated with its NASTAR Center.

8. Long-Term Obligations and Credit Arrangements:

Lenfest Letter Agreement

Effective May 9, 2007, the Company entered into a letter agreement with H.F. Lenfest ("the Lenfest Letter Agreement") whereas Mr. Lenfest agreed to provide financial support to the Company in the form of a guarantee and/or provide access to funding until June 30, 2008. The Company is currently in negotiations with an institutional lender in connection with a proposed facility which would require the personal guarantee of Mr. Lenfest. If successful, the proposed facility would replace the Company's current equity credit line and unsecured promissory note with Mr. Lenfest. Alternately, Mr. Lenfest has agreed to maintain his existing financial arrangements with the Company and in addition provide additional funding, provided that the Company shall not request more than an additional $10 million in the aggregate from the date of the Lenfest Letter Agreement through June 30, 2008, including all requests made under the existing $3 million unsecured promissory note and the $15 million equity credit line.

Long-term obligations at February 23, 2007 and February 24, 2006 consist of the following:

	(amounts in thousands) 2007	2006
Credit facility payable to banks	$ —	$ —
Subordinated convertible debt, net of unamortized discount of $1,170 and $1,624 for 2007 and 2006, respectively	8,830	8,376
	8,830	8,376
Less current portion	—	—
	$ 8,830	$ 8,376

The amounts of future long-term obligations maturing in each of the next five fiscal years are as follows (amounts in thousands):

2008	—
2009	8,830
2010	—
2011	—
2012 and thereafter	—
Total future obligations	$ 8,830

The approximate average loan balance, maximum aggregate borrowings outstanding at any month-end payable under the credit facility and subordinated debt during the fiscal years, and weighted average interest rate computed by the day's outstanding method as of February 24, 2006 and February 25, 2005 are as follows (amounts in thousands):

	2007	2006
Approximate average loan balance (face)	10,000	10,000
Maximum aggregate	10,000	10,000
Weighted average interest rate	8.00%*	8.00%*

* The interest rate in the Company's subordinated debt agreement is 10% per annum. However, Mr. Lenfest reduced the interest rate to 8% per annum on a temporary basis for the period December 1, 2004 through November 30, 2007.

Refinancing

The Company has historically financed operations through a combination of cash generated from operations, equity offerings, subordinated borrowings and bank debt. On February 19, 2003, the Company refinanced its outstanding indebtedness (the "Refinancing"). The Refinancing was effected through the issuance of subordinated, convertible notes to H.F. Lenfest, a Director of the Company, and a credit agreement (the "PNC Agreement") with PNC Bank, National Association ("PNC"). The total proceeds from the Refinancing were $29,800,000.

Bank Credit and Facility

Since inception, the PNC Agreement has had numerous amendments. As of fiscal 2007-year end, the facility total was $5,000,000 and use of this amount was restricted to the issuance of international letters of credit. This line was secured by all assets of the Company as well as a $5,000,000 personal guarantee by Mr. Lenfest.

On November 16, 2006, we entered into a Letter Agreement with PNC Bank. This Letter Agreement amended, restated and replaced the existing PNC Agreement. Pursuant to the Letter Agreement, PNC Bank (i) terminated our Credit Agreement dated as of February 18, 2003 (ii) re-approved our $5 million Line of Credit for Letters of Credit, and (iii) re-affirmed the Tangible Net Worth covenant (as defined in the Letter Agreement) to a be a minimum of $9,000,000. The $5 million Line of Credit for Letters of Credit continued to be guaranteed by Mr. Lenfest. As of February 23, 2007, we had used approximately $2,607,000 of the availability under the PNC Agreement for international letters of credit.

Equity Line

On April 7, 2006, the Company entered into a Preferred Stock Purchase Agreement (the "Lenfest Equity Agreement") with Mr. Lenfest. The Lenfest Equity Agreement, which terminates on October 6, 2007, permitted ETC to unilaterally draw down up to $15 million in exchange for shares of the Company's Series B Cumulative Convertible Preferred Stock ("Preferred Stock"). The Preferred Stock provides for a dividend equal to six percent per annum. After three years, the Preferred Stock will be convertible, at Mr. Lenfest's request, into ETC common shares at a conversion price (the "Conversion Price") which will be set on the day of each draw down. The Conversion Price will be equal to the closing price of the Company's common stock on the trading day immediately preceding the day in which the draw down occurs, subject to a floor price of $4.95 per common share. Drawdowns will not be permitted on any day when the Conversion Price would be less than this floor price. On the sixth anniversary of the Lenfest Equity Agreement, any issued and outstanding Preferred Stock will be mandatorily converted into ETC common stock at each set Conversion Price. The Lenfest Equity Agreement also allows for the Company to redeem any outstanding Preferred Stock any time within the six year term of the Lenfest Equity Agreement. The Preferred

Stock will vote with the ETC common stock on an as converted basis. In connection with the execution of the Lenfest Equity Agreement, the Company drew down $3 million by issuing 3,000 shares of Preferred Stock with a Conversion Price equal to $4.95 per share. Additionally, on July 31, 2006, we drew down an additional $3 million by issuing 3,000 shares of Preferred Stock at a conversion price equal to $6.68 per common share.

Unsecured Note

On November 16, 2006, the Company executed an Unsecured Promissory Note (the “Lenfest Note”) in favor of Mr. Lenfest in the aggregate principal amount of $3,000,000. Pursuant to the terms of the Lenfest Note, ETC can borrow up to $3,000,000, in increments of $1,000,000, prior to the maturity date of October 6, 2007. As of the date of this filing on Form 10-K, ETC owed $2,000,000 under the Lenfest Note.

All outstanding and unpaid interest on the Lenfest Note is due and payable on the earlier of (i) October 6, 2007 or (ii) such date as ETC draws down funds sufficient to repay the amount due under the Lenfest Note pursuant to the Lenfest Equity Agreement.

Borrowings made pursuant to the Lenfest Note bear interest at an annual rate of six percent with such interest beginning to accrue on the date of the funding of each loan and, to the extent not paid, compounding on the first day of each month.

The Lenfest Note provides for customary events of default including, but not limited to, the nonpayment of any amount payable when due, certain bankruptcy, insolvency or receivership events and the imposition of certain judgments. Upon the occurrence of an event of default, Mr. Lenfest has the right to accelerate the maturity date of the Lenfest Note and demand immediate payment of all amounts payable there under.

Subordinated Convertible Debt

In connection with the financing provided by PNC Bank on February 19, 2003, the Company entered into a Convertible Note and Warrant Purchase Agreement with Mr. Lenfest (the “Subordinated Note”), pursuant to which the Company issued to Mr. Lenfest (i) a senior subordinated convertible promissory note in the original principal amount of $10,000,000 and (ii) warrants to purchase 803,048 shares of the Company’s common stock. Upon the occurrence of certain events, the Company will be obligated to issue additional warrants to Mr. Lenfest. The Subordinated Note accrues interest at the rate of 10% per annum (Mr. Lenfest reduced the rate to 8% on a temporary basis for the period December 1, 2004 through November 30, 2007) and matures on February 18, 2009. At the Company’s option, the quarterly interest payments may be deferred and added to the outstanding principal. The Subordinated Note entitles Mr. Lenfest to convert all or a portion of the outstanding principal of, and accrued and unpaid interest on, the note into shares of ETC common stock at a conversion price of $6.05 per share. The warrants may be exercised into shares of ETC common stock at an exercise price equal to the lesser of $4.00 per share or two-thirds of the average of the high and low sale prices of the ETC common stock for the 25 consecutive trading days immediately preceding the date of exercise.

The obligations of the Company to Mr. Lenfest under the Subordinated Note are secured by a second lien on all of the assets of the Company, junior in rights to the lien in favor of PNC Bank, including all real property owned by the Company.

Subordinated Convertible Debt Discount

During fiscal 2003, the Company had recorded $2,609,000 in additional paid-in capital representing an allocation of the proceeds from the convertible debt element of its financing with PNC Bank and Lenfest. This allocation represents the value assigned to the beneficial conversion option of the promissory note executed in favor of Mr. Lenfest and the value of the associated warrants issued in connection with the Refinancing. Such values were derived pursuant to an independent appraisal of these financial instruments obtained by the Company. Accreted interest expense related to the beneficial conversion option and the warrants was $454,000, $384,000 and $326,000 in fiscal 2007, fiscal 2006 and 2005, respectively.

The following table summarizes the subordinated convertible debt as of February 23, 2007 (amounts in thousands):

Face Value	$ 10,000
Less value of conversion feature	(1,400)
Less value of warrants	(1,209)
	7,391
Accretion 2007	454
Accretion 2006	384
Accretion 2005	326
Accretion 2004	275
Carrying value at February 23, 2007	$ 8,830

Interest expense recorded for these notes was $802,000 and $803,000 for fiscal 2007 and 2006, respectively.

Fair Value

The carrying value of these financial instruments approximates their fair values at February 23, 2007.

Prior to the consummation of the Refinancing, Advanced Technology Asset Management, LLC (“ATAM”) (formerly ETC Asset Management, LLC), a shareholder of the Company and a holder of warrants to purchase 332,820 shares of the Company’s common stock, consented to the transactions contemplated under the PNC Agreement and the financing provided by Mr. Lenfest, including the below market issuance of warrants to Mr. Lenfest. As a result of its consent, ATAM waived, solely in connection with such issuance, the anti-dilution rights contained in its warrant. In exchange for ATAM’s consent, the Company issued to ATAM warrants to purchase an additional 105,000 shares of common stock. Except for the number of shares issuable upon exercise of the warrants, the new ATAM warrants contained substantially the same terms as the warrants issued to Mr. Lenfest. In March 2004, ATAM exercised all of its warrants and received a total of 437,820 shares of common stock of the Company. The Company received proceeds of $586,410 from the exercise of these warrants.

As a condition of amending the PNC Agreement on August 24, 2004, Mr. Lenfest agreed to issue to PNC Bank on the Company’s behalf a limited guarantee to secure up to $5,000,000 in principal amount of any letters of credit issued under the amended facility. In consideration for issuing this guarantee, Mr.Lenfest will receive a fee of 0.75% per annum of the average amount of letters of credit outstanding, payable on a quarterly basis, and did receive a warrant to purchase 200,000 shares of stock under the same terms and conditions as the warrant issued to Mr. Lenfest in connection with the Refinancing.

On February 14, 2005, Mr. Lenfest exercised all of his outstanding warrants and received 1,003,048 shares of ETC common stock for approximately $3.9 million. Additionally, on February 14, 2005, Mr. Lenfest purchased 373,831 shares of the Company’s common stock for approximately $2.0 million.

Under the Note, the Company must meet certain financial covenants including a Leverage Ratio, a Fixed Charge Ratio and a Tangible Net Worth Ratio. At February 23, 2007 the Company failed to meet any of these financial covenants but has obtained a waiver from Mr. Lenfest. This waiver applies to the period through February 24, 2008. Except as specified, the waiver does not constitute a modification or alteration of any other terms or conditions in the Note, or a release of any of the lender’s rights or remedies, all of which are reserved, nor does it release the Company or any guarantor from any of its duties, obligations, covenants or agreements including the consequences of any Event of Default, except as specified.

Long-Term Bonds

On March 15, 2000, the Company issued approximately $5,500,000 of unregistered Taxable Variable Rate Demand/Fixed Rate Revenue Bonds (Series of 2000). Net proceeds from these bonds were used to repay a $4,100,000 advance taken on the Company’s revolving credit facility and to finance construction of an addition to the Company’s main plant in Southampton, Pennsylvania. The bonds were secured by a $5,000,000 irrevocable direct pay Letter of Credit issued by PNC Bank which was scheduled to expire on February 17, 2006 and which was secured by all assets of the Company. At February 25, 2005, the bonds were fully cash collateralized. The bonds carried a maturity date of April 1, 2020, bore a variable interest rate which adjusted each week to a rate required to remarket

the bonds at full principal value with a cap of 17%, and were subject to mandatory redemption of $275,000 per year for 19 years and $245,000 for the 20th year.

On June 30, 2005, the Company directed the trustee for the bonds to issue a redemption notice for all of the Company's outstanding bonds. On August 1, 2005, the Company utilized the restricted cash held by PNC Bank to redeem all outstanding bonds. As of May 27, 2005, all deferred financing charges associated with this bond issue had been fully amortized to the Company's statement of operations.

Liquidity

Given the Company's inability to borrow cash under the amended PNC Agreement and certain restrictions in the Lenfest Equity Agreement, the Company may need to obtain additional sources of capital in order to continue growing and operating its business. This capital may be difficult to obtain and the cost of this additional capital is likely to be relatively high. However, because we have established businesses in many markets, significant fixed assets including a building, and other valuable business assets which can be used for security, we believe that we will be able to locate such additional capital and that the actions by PNC Bank will not have a long-term material adverse effect on our business.

We believe that existing cash balances at February 23, 2007, cash generated from operating activities, future availability under either the Lenfest Equity Agreement, the Lenfest Note or the Letter Agreement with Mr. Lenfest and/or other arrangements with other lenders or investors will be adequate to meet our future obligations through at least March 1, 2008.

In reference to the Company's outstanding claims with the U.S. Government, to the extent the Company is unsuccessful in recovering a significant portion of recorded claim contract costs, and to the extent that significant additional legal expenses are required to bring the dispute to resolution, such events could have a material adverse effect on the Company's liquidity and results of operations. Historically, the Company has had a favorable experience in that recoveries have exceeded recorded claims, including significant settlement agreements in fiscal 2003, 2004 and 2005. However, this claim was filed in the Court of Federal Appeals whereas prior government claims were filed with the Armed Services Board of Contract Appeals (ASBCA), which has complicated the litigation process. (See Note 4 to the Consolidated Financial Statements, Accounts Receivable).

9. Leases:

Operating Leases

The Company leases certain premises and office equipment under operating leases, which expire over the next five years. Future minimum rental payments required under noncancellable operating leases having a remaining term expiring after one fiscal year as of February 23, 2007 are $129,000 in 2008; $132,000 in 2009; $133,000 in 2010; $131,000 in 2011; and $94,000 in 2012 and thereafter.

Total rental expense for all operating leases for the fiscal years ended February 23, 2007, February 24, 2006 and February 25 2005 was $177,000, $173,000 and $198,000, respectively.

10. Income Taxes:

The components of the provision for income taxes are as follows:

	(amounts in thousands)		
	52 Weeks Ended February 23, 2007	52 Weeks Ended February 24, 2006	52 Weeks Ended February 25, 2005
Currently (receivable)/payable:			
Federal	$ —	$ —	$ (909)
State	—	—	—
Foreign (benefit) taxes	(6)	136	(44)
	(6)	136	(953)
Deferred:			
Federal	—	—	(198)
State	—	—	34
Foreign benefit	(71)	—	—
	—	—	(165)
	$ (77)	$ 136	$ (1,117)

A reconciliation of the statutory federal income tax rate to the effective tax rate is as follows:

	52 Weeks Ended February 23, 2007	52 Weeks Ended February 24, 2006	52 Weeks Ended February 25, 2005
Statutory income tax	(34.0)%	(34.0)%	(34.0)%
State income tax, net of federal tax benefit	(0.0)	(4.6)	0.2
Research and experimentation and other tax credits	(1.6)	(2.6)	(1.6)
Benefit of foreign and foreign-source income or loss	(0.9)	1.2	(0.3)
Change in valuation allowance	35.1	41.9	24.3
Other, net	0.5	0.1	(0.8)
	(0.9)%	2.1%	(12.2%)

The tax effects of the primary temporary differences are as follows:

	(amounts in thousands)		
	2007	2006	2005
Deferred tax assets:			
Vacation reserve	66	64	51
Inventory reserve	317	330	214
Receivable reserve	137	368	184
Warranty reserve	63	8	8
Compensation and other reserves	114	132	136
Stock options	96	—	—
Net operating loss and credits	8,536	5,436	3,172
Other, net	82	200	252
	9,411	6,538	4,017
Valuation Reserve	(8,149)	(4,980)	(2,231)
Total current deferred tax asset	$ 1,262	$ 1,558	$ 1,786
Deferred tax liabilities:			
Amortization of capitalized software	$ 886	$ 1,175	$ 1,419
Depreciation	305	383	367
Total non-current deferred tax liability	$ 1,191	$ 1,558	$ 1,786

Reflecting the Company's significant losses in the current and prior fiscal years, the Company has approximately $20.5 million of federal net loss carry forwards available to offset future income tax liabilities, beginning to expire in 2025. However, due to the uncertain nature of their ultimate realization based on past performance, and the potential that sufficient taxable income may not be generated in the near future, the Company has established a full valuation allowance of the same amount against these carry forward benefits and will recognize these benefits only as reassessment demonstrates that they are realizable. Realization is entirely dependent upon future earnings in specific tax jurisdictions. While the need for this valuation allowance is subject to periodic review, if the allowance is reduced, the tax benefits of the carry forwards will be recorded in future operations as a reduction of the Company's income tax expense. In addition, the Company may be subject to a limitation on the use of its net operating losses based on potential ownership changes that may have occurred as defined by Section 382 of the Internal Revenue Code. The Company is currently evaluating the need to undertake an ownership change study in order to conclude if a further limitation is required.

11. Business Segment Information:

The Company primarily manufactures, under contract, various types of high-technology equipment which it has designed and developed. The Company considers its business activities to be divided into two segments: Training Services Group (TSG) (formerly Aircrew Training Systems) and the Control Systems Group (CSG) (formerly Industrial Group). The TSG business produces devices which create and monitor the physiological effects of motion, including spatial disorientation and centrifugal forces for medical, training, research and entertainment markets. The CSG business produces chambers that create environments that are used for sterilization, research and medical applications. The following segment information reflects the accrual basis of accounting.

(amounts in thousands)

	Training Services TSG	Control Systems CSG	Total
Fiscal 2007			
Net sales	$ 9,293	$ 8,126	$ 17,419
Interest expense	852	299	1,151
Depreciation and amortization	973	884	1,857
Operating loss	(3,991)	(2,724)	(6,715)
Income tax benefit	(77)	—	(77)
Goodwill	455	—	455
Identifiable assets	7,698	7,113	14,811
Expenditures for segment assets	160	148	308
Fiscal 2006			
Net sales	$ 15,100	$ 9,969	$25,069
Interest expense	1,265	592	1,857
Depreciation and amortization	1,533	1,037	2,570
Operating loss	(3,555)	(362)	(3,917)
Income tax expense	136	—	136
Goodwill	455	—	455
Identifiable assets	15,809	7,407	23,216
Expenditures for segment assets	234	109	343
Fiscal 2005			
Net sales	$ 16,788	$ 11,026	$ 27,814
Interest expense	1,189	602	1,791
Depreciation and amortization	1,337	1,078	2,415
Operating loss	(4,768)	(1,518)	(6,286)
Income tax benefit	(715)	(254)	(969)
Goodwill	477	—	477
Identifiable assets	14,899	7,947	22,846
Expenditures for segment assets	228	57	285

	2007	2006	2005
Reconciliation to consolidated amounts:			
Corporate assets	16,709	10,451	25,063
Total assets	$ 31,520	$ 33,667	$ 47,909
Segment operating (loss)/income	$ (6,715)	$ (3,917)	$ (6,286)
Less interest expense	(1,151)	(1,857)	(1,791)
Income tax (provision) benefit	77	(136)	969
Total loss for segments	(7,789)	(5,910)	(7,108)
Corporate home office expense	(1,217)	(802)	(846)

Interest and other expenses	58	15	(308)
Income tax benefit	—	—	149
Minority interest	8	(17)	—
Net loss	$ (8,940)	$ (6,714)	$ (8,113)

Segment operating income consists of net sales less applicable costs and expenses relating to these revenues. Unallocated expenses including general corporate expenses, letter of credit fees, interest expense, and income taxes have been excluded from the determination of the total profit for segments. General corporate expenses are primarily central administrative office expenses. Property, plant, and equipment are not identified with specific business segments because most of these assets are used in each of the segments.

In fiscal 2007, international sales totaling at least ten percent of total international sales were made to one customer in Japan for $3,365,000. In fiscal 2006, international sales totaling at least ten percent of total international sales were made in the Company's Polish subsidiary to L-3 Communications ($4,599,000) and to a government customer in Pakistan ($2,910,000). In fiscal 2005, international sales totaling at least ten percent of total international sales were made to government or commercial accounts in Malaysia ($3,388,000) and Egypt ($2,309,000). Fluctuations in sales to international countries from year to year primarily reflect revenue recognition on the level and stage of development and production on multi-year long-term contracts.

Approximately 26% of sales totaling $4,465,000 in fiscal 2007 were made to two customers, one customer in Japan (TSG segment) and one domestic customer (CSG segment). Approximately 30% of sales totaling $7,509,000 in fiscal 2006 were made to two customers, one from our Polish subsidiary and one international customer from our domestic operation, in the TSG segment. Approximately 20% of sales totaling $5,697,000 in fiscal 2005 were made to two international customers in the TSG segment.

Included in the segment information for the year ended February 23, 2007, are export sales of $10,821,000. Of this amount, there are sales to or relating to governments or commercial accounts in Japan of $3,365,000. Sales to the U.S. government and its agencies aggregated $586,000 for the year ended February 23, 2007.

Included in the segment information for the year ended February 24, 2006, are export sales of $13,343,000. Of this amount, there are sales to or relating to governments or commercial accounts in Pakistan of $2,910,000. Sales to the U.S. government and its agencies aggregated $2,586,000 for the year ended February 24, 2006.

Included in the segment information for the year ended February 25, 2005, are export sales of $12,912,000. Of this amount, there are sales to or relating to governments or commercial accounts in Malaysia of $3,388,000 and Egypt of $2,309,000. Sales to the U.S. government and its agencies aggregated $2,904,000 for the year ended February 25, 2005.

12. Stock Options:

A summary of the status of the Company's Stock Option Plans as of and for the fiscal years ended:

	February 23, 2007		February 24, 2006		February 25, 2005	
	Shares	Weighted average Exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding at beginning of year	247,939	$ 7.31	276,162	$ 7.30	376,002	$ 7.21
Granted	124,639	5.46	—	—	33,586	7.24
Exercised	(650)	3.31	(1,600)	6.35	(25,700)	6.35
Forfeited	—	—	(26,623)	7.18	(107,726)	7.18
Outstanding at end of year	371,928	6.70	247,939	7.31	276,162	7.30
Options exercisable at year end	310,496		222,750		242,576	
Weighted average fair value of options granted during the year		$ 6.76		3.58		$ 3.58

The following information applies to options outstanding at February 23, 2007:

	Options outstanding			Options exercisable	
Range of exercise prices	Number Outstanding at February 23, 2007	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable at February 23, 2007	Weighted average exercise price
$5.00 to $5.12	114,500	6.7 years	$ 5.08	114,500	$ 5.08
$7.24 to $7.81	257,428	3.8 years	$ 7.41	195,996	$ 7.73
Total	371,928			310,496	

13. Commitments and Contingencies

Claims and Litigation:

In June 2003, Entertainment Technology Corporation (“EnTCo”), our wholly-owned subsidiary, filed suit against Walt Disney World Co. and other entities (“Disney”) in the United States District Court for the Eastern District of Pennsylvania, alleging breach of contract for, among other things, failure to pay all amounts due under contract for the design and production of the amusement park ride “Mission: Space” located in Disney’s Epcot Center. In response, in August 2003, Disney filed counterclaims against both EnTCo and us (under a guarantee) for, among other things, alleged failures in performance and design in the contract. Disney is seeking damages in excess of $65 million plus punitive damages. In December 2005, EnTCo filed a second suit against Disney, alleging breach of confidentiality and unfair trade practices. Both EnTCo and we believe that we have valid defenses to each of Disney’s counterclaims and intend to vigorously defend ourselves against these counterclaims. . Discovery is expected to be completed by June 2007 with pre-trial motions to follow. The case is not currently scheduled for trial. Neither EnTCo nor we are able to predict the outcome of this matter.

In May 2003 we filed a certified claim with the Department of the Navy seeking costs totaling in excess of $5.0 million in connection with a contract for a submarine rescue decompression chamber project. This claim against the Navy has followed the typical process of claim notification, preparation, submittal, government audit and review by the contracting officer. On July 22, 2004, the Navy’s Contracting Officer issued a final decision denying the claim in full. In July 2005, we converted this claim into a complaint, which we filed in the Court of Federal Claims. This case is currently scheduled for trial in July 2007. While we intend to vigorously litigate this case, we cannot predict the outcome of this matter and an unfavorable result could have a material adverse effect on our financial position.

Certain other claims, suits, and complaints arising in the ordinary course of business have been filed or are pending against us. In our opinion, after consultation with legal counsel handling these specific maters, all such matters are reserved for or adequately covered by insurance or, if not so covered, are without merit or are of such kind, or involve such amounts, as would not have a significant effect on our financial position or results of operations if disposed of unfavorably.

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14. Employee Benefit Plan:

The Company maintains a retirement savings 401(k) plan for eligible employees. The Company’s contributions to the plan are based on a percentage of the employees’ qualifying contributions. The Company’s contributions totaled $112,000, $110,000 and $106,000 in fiscal 2007, fiscal 2006, and fiscal 2005, respectively.

The Company has an Employee Stock Purchase Plan, which was adopted by the Board of Directors on November 3, 1987. All employees meeting service requirements, except officers, directors and 10% shareholders, are eligible to voluntarily purchase common stock through payroll deductions up to 10% of salary. The Company makes a matching contribution of 20% of the employee’s contribution. The Company has reserved 270,000 shares for issuance under the plan.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

15. Quarterly Consolidated Financial Information (Unaudited):

Financial data for the interim periods of fiscal 2007, 2006 and 2005 were as follows (amounts in thousands):

	Quarter ended:			
Fiscal Year 2007	**May 26**	**August 25**	**November 24**	**February 23**
Net sales	$4,575	$ 4,329	$ 4,718	$ 3,797
Gross profit (loss)	1,014	494	1,030	(467)
Operating loss	(1,701)	(1,913)	(1,581)	(2,737)
Loss before income taxes	(2,033)	(2,154)	(1,829)	(3,009)
Minority interest	(8)	(16)	33	(23)
Net loss	(2,030)	(2,148)	(1,866)	(2,896)
Loss per common share:				
Basic	($0.23)	($0.24)	($0.22)	($0.33)
Diluted	($0.23)	($0.24)	($0.22)	($0.33)

	Quarter ended:			
Fiscal Year 2006	**May 27**	**August 26**	**November 25**	**February 24**
Net sales	$5,915	$6,255	$ 6,206	$ 6,693
Gross profit	1,482	1,253	1,367	1,248
Operating loss	(1,152)	(1,149)	(986)	(1,410)
Loss before income taxes	(1,726)	(1,619)	(1,317)	(1,899)
Minority interest	(3)	1	6	13
Net loss	(1,723)	(1,620)	(1,327)	(2,044)
Loss per common share:				
Basic	($0.19)	($0.18)	($0.15)	($0.23)
Diluted	($0.19)	($0.18)	($0.15)	($0.23)

	Quarter ended:			
Fiscal Year 2005	**May 28**	**August 27**	**November 26**	**February 25**
Net sales	$ 6,175	$ 6,523	$ 7,751	$ 7,365
Gross profit	994	1,021	1,637	2,524
Operating loss	(1,645)	(2,392)	(2,757)	(336)
Loss before income taxes	(2,074)	(2,819)	(3,254)	(1,082)
Minority interest	1	0	(1)	0
Net loss	(1,461)	(1,984)	(3,249)	(1,419)
Loss per common share:				
Basic	($0.19)	($0.26)	($0.43)	($0.18)
Diluted	($0.19)	($0.26)	($0.43)	($0.18)

ENVIRONMENTAL TECTONICS CORPORATION AND SUBSIDIARIES
SCHEDULE II
VALUATION AND QUALIFYING ACCOUNTS
(amounts in thousands)

Column A	Column B	Column C	Column D	Column E
Description	Balance at beginning of period	Charges / (credits) to costs or expenses	Reductions	Balance at end of period
Fiscal year ended February 23, 2007				
Valuation and qualifying accounts related to:				
Accounts receivable	$ 965	$ 18	$ 615	$ 368
Inventory	1,032	446	487	991
Property, plant and equipment	12,134	626	—	12,760
Software development costs	9,882	1,231	—	11,113
Fiscal year ended February 24, 2006				
Valuation and qualifying accounts related to:				
Accounts receivable	$ 486	$ 510	$ 31	$ 965
Inventory	731	823	522	1,032
Property, plant and equipment	11,491	643	—	12,134
Software development costs	8,658	1,224	—	9,882
Other assets	1,180	—	725	455
Fiscal year ended February 25, 2005				
Valuation and qualifying accounts related to:				
Accounts receivable	$ 379	$ 126	$ 19	$ 486
Inventory	564	300	133	731
Property, plant and equipment	10,651	840	—	11,491
Software development costs	7,670	988	—	8,658
Other assets	434	746	—	1,180

Environmental Tectonics Corporation

Code of Ethics

Chief Executive Officer and Senior Financial Officers

The Company's Chief Executive Officer ("CEO") and senior financial officers hold important and elevated roles in corporate governance in that they are uniquely capable and empowered to ensure that shareholders, creditors and other stakeholders' interests are appropriately balanced, protected and preserved. This policy emphasizes the role of the CEO and senior financial officers in the conduct and practice of financial management and provides that the CEO and senior financial officers shall follow and advocate.

SENIOR FINANCIAL OFFICERS

Senior financial officers include the Company's Chief Financial Officer ("CEO"), Controller, and the chairperson of the Company's disclosure committee should those positions exist by name or responsibility.

HONESTY AND INTEGRITY

The CEO and senior financial officers shall observe high standards of business and personal ethics and practice honesty and integrity in every respect of dealing with the public, the business community, stockholders and government authorities.

COMPLIANCE WITH LAWS AND REGULATIONS

The CEO and senior financial officers shall comply with applicable laws, regulations and related rules and are prohibited from engaging in any activities that could involve the Company in any unlawful practice.

AVOIDANCE OF CONFLICTS OF INTERESTS

The CEO and senior financial officers shall not engage in apparent, potential or actual conflicts of interest, improper solicitation of business, conflicts based on outside interests and political contributions of Company funds.

FULL, FAIR, ACCURATE, TIMELY AND UNDERSTANDABLE FINANCIAL DISCLOSURE

The CEO and senior financial officers are responsible for the Company's accounting controls and procedures, and the protection of shareholder interests. The responsibility includes the full, fair, accurate, timely and understandable disclosure in reports and documents filed or submitted to the Securities and Exchange Commission, American Stock Exchange, public communications made by the Company, other regulatory or required reports and internal reports.

COMPLIANCE

The CEO and senior financial officers shall comply with this Code and the ETC Code of Conduct. Failure to comply with this Code or the ETC Code of Conduct will result in appropriate sanctions administered with principles of fairness and equity, up to and including termination of employment.

EXHIBIT 21

List of Subsidiaries

Name	Jurisdiction	% Ownership
Entertainment Technology Corporation	PA	100%
ETC International Corporation	Barbados	100%
ETC-PZL Aerospace Industries	Poland	9 5%
ETC-Europe	Great Britain	9 9%
ETC-Delaware	Delaware	100%
NASTAR Center Holdings Corporation	Delaware	100%
NASTAR Center LLC	Delaware	100%

EXHIBIT 23

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our report dated May 21, 2007, accompanying the consolidated financial statements and schedule incorporated by reference in the Annual Report of Environmental Tectonics Corporation and Subsidiaries on Form 10-K for the year ended February 23, 2007. We hereby consent to the incorporation by reference of said report in the Registration Statements of Environmental Tectonics Corporation and Subsidiaries on Forms S-8 (File No. 333-131322, effective January 27, 2006, File No. 333-65469, effective October 8, 1998 and File No. 2-92407, effective August 14, 1984), Form S-3A (File No. 333-29083, effective July 2, 1997) and Forms S-3 (File No. 333-29083, effective June 12, 1997 and File No. 33-42219, effective September 4, 1991).

/s/Grant Thornton LLP
Philadelphia, Pennsylvania
May 21, 2007

EXHIBIT 31.1

CERTIFICATION PURSUANT TO RULE 13A-14(A) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, William F. Mitchell, certify that:

1. I have reviewed this Annual Report on Form 10-K of Environmental Tectonics Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 24, 2007

By: /s/ William F. Mitchell
William F. Mitchell
President and Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION PURSUANT TO RULE 13A-14(A) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, Duane D. Deaner, certify that:

1. I have reviewed this Annual Report on Form 10-K of Environmental Tectonics Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 24, 2007

By: /s/ Duane D. Deaner
Duane D. Deaner
Chief Financial Officer

EXHIBIT 32

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Environmental Tectonics Corporation (the "Company") for the fiscal year ended February 23, 2007 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William F. Mitchell, Chief Executive Officer of the Company, and I, Duane D. Deaner, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

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

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/William F. Mitchell
William F. Mitchell
Chief Executive Officer

/s/ Duane D. Deaner
Duane D. Deaner
Chief Financial Officer

May 24, 2007

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed to be filed by the Company for purpose of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

EXHIBIT 10.33

EXECUTIVE EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the “Agreement”) is entered into between Duane D. Deaner (“Executive”) and Environmental Tectonics Corporation (the “Company”), collectively referred to as the “Parties,” with an “Effective Date” of November 1, 2005.

1. Executive’s Position/Duties. During the term of this Agreement, Executive will be employed as the Chief Financial Officer of the Company, and shall have all of the duties and responsibilities of that position. Executive shall be considered a key employee of the Company and shall be entitled to all the Company benefits afforded to key employees. Executive agrees to dedicate all of his working time (during normal working hours other than during excused absences such as for illness or vacation), skill and attention to the business of the Company, agrees to remain loyal to the Company, and not to engage in any conduct that creates a conflict of interest to, or damages the reputation of, the Company.

2. Term of Employment. The term of this Agreement shall be for a period of two years. Executive’s employment under this Agreement will commence on the Effective Date, and will continue for a period of two years, unless terminated earlier in accordance with the provisions of this Agreement. The Company shall, at least six months prior to each scheduled expiration of this Agreement, provide Executive with written acknowledgment of the renewal of Executive’s employment with the Company for a period of two years from the end of the current term (the “Acknowledgement”). If the Company fails to provide the Acknowledgement, and such failure is not cured within ten (10) days of the Company receiving notice by Executive of

this failure, the Executive shall be entitled to terminate his employment with the Company pursuant to Section 4 and receive the benefits set forth in Section 5(a).

3. Compensation.

(a) Base Salary. During the term of this Agreement, the Company shall provide Executive with a base salary ("Base Salary") as shall be determined by the President of the Company (the "President") and as set forth on Exhibit "A" hereto; provided, however, that such Base Salary shall not be reduced unless such reduction is pursuant and proportionate to a company-wide reduction ("Salary Reduction") of all base salaries for management personnel. Base Salary shall be subject to increase (a "Salary Increase") based on Executive's annual performance review as conducted by the President. Base Salary shall be paid in accordance with the Company's normal payroll policies.

(b) Bonuses/Distributions. Each year during the term of this Agreement, the Company shall provide Executive with a bonus based on the formula and targets established under and in accordance with the Company's Key Management Bonus Plan to be set forth on Exhibit "B" hereto and as administered by the President. Executive may receive additional bonuses at the discretion of the President.

(c) Benefits. Executive shall be entitled to all benefits, including, but not limited to participation in any compensation plan, health, dental and insurance program, pension plans, profit sharing, vacation, sick leave, expense accounts, and retirement benefit, all as afforded other management personnel or as determined by the President.

(d) Expenses. The Company shall reimburse Executive for reasonable expenses incurred in the performance of his duties and services hereunder and in furtherance of

the business of the Company, in accordance with the policies and procedures established by the Company.

4. Termination of Employment. Executive's employment with the Company may be terminated as follows:

(a) Death. In the event of Executive's death, Executive's employment will be terminated immediately.

(b) Disability. In the event of Executive's Disability, as defined below, Executive's employment will be terminated upon thirty-days (30) written notice. "Disability" shall mean a written determination by a physician mutually agreeable to the Company and Executive (or, in the event of Executive's total physical or mental disability, Executive's legal representative) that Executive is physically or mentally unable to perform his duties as Chief Financial Officer under this Agreement and that such disability can reasonably be expected to continue for a period of six (6) consecutive months or for shorter periods aggregating one hundred eighty (180) days in any 12-month period.

(c) Termination by the Company for Cause or by Executive without Good Reason . The Company shall be entitled to terminate Executive's employment upon thirty (30) days written notice if it has "Cause," which shall mean any of the following: (i) a documented repeated and willful failure by Executive to perform his duties, but only after the President's written demand and only if termination is effected by action taken by a vote of (A) prior to a Change in Control (as defined below), at least a majority of the directors of the Company then in office, or (B) after a Change in Control, at least 80% of the non-officer directors then in office of the Company, (ii) Executive is convicted of a felony or enters a plea of guilty or nolo contendere to a felony, a crime of falsehood or a crime involving fraud or moral turpitude or the actual

incarceration of Executive for at least forty-five (45) consecutive days, (iii) conduct by Executive constituting moral turpitude, or (iv) conduct by Executive involving dishonesty in business dealings that are directly and materially injurious to the Company. Executive shall also be entitled to terminate this Agreement upon thirty-days (30) written notice without Good Reason (as defined herein).

(d) Without Cause. Either the Company or Executive may terminate Executive's employment at any time without cause upon ninety (90) days written notice; provided, however, that if a Change of Control has occurred Executive may terminate his employment upon thirty (30) days written notice.

(e) Termination by Executive with Good Reason. Executive shall be entitled to terminate his employment upon thirty (30) days written notice after the occurrence of any of the following events (each of which shall constitute "Good Reason"):

(i) prior to a Change in Control:

A. a change in Executive's status or position, or any material diminution in his duties or responsibilities;

B. a reduction in Base Salary, other than a Salary Reduction;

C. a failure to increase Base Salary consistent with Executive's performance review within a twenty-four (24) month period since the previous Salary Increase; provided, however, that such period shall not apply if there are no increases of base salaries on a company-wide basis for the Company's management personnel or if there is a voluntary deferral by Executive of the last Company offered Salary Increase;

D. failure of the Company, which is not cured within ten (10) days of receiving notice by Executive of such failure, to deliver the Acknowledgment to

Executive at least six months prior to any scheduled expiration of the Agreement; or

E. any purported termination of Executive's employment which is not in accordance with the terms of this Agreement; and

(ii) after a Change in Control:

A. a change in Executive's status or position, or any material diminution in his duties or responsibilities;

B. any increase in Executive's duties inconsistent with his position;

C. any reduction in Base Salary;

D. a failure to increase Base Salary consistent with Executive's performance review within a twelve (12) month period since the most recent of either the last Salary Increase or the Executive's most recent performance review;

E. a failure to continue in effect any Employee Benefit Plan (as such term is defined in the Employee Retirement Income Security Act of 1974 ("ERISA"), Section 3(3)) in which Executive participates, including (whether or not they constitute Employee Benefit Plans) incentive bonus, stock option, or other qualified or nonqualified plans of deferred compensation (x) other than as a result of the normal expiration of such a plan, or (y) unless such plan is merged or consolidated into, or replaced with, a plan with benefits which are of equal or greater value;

F. requiring Executive to be based anywhere other than the county where their principal office was located immediately prior to the Change in Control;

G. refusal to allow the Executive to attend to matters or engage in activities in which he was permitted to engage prior to the Change in Control;

H. failure of the Company, which is not cured within ten (10) days of receiving notice by Executive of such failure, to deliver the Acknowledgment to Executive at least six months prior to any scheduled expiration of the Agreement;

I. failure to secure the affirmation by a Successor, within three (3) business days prior to a Change in Control, of this Agreement and the continuing obligations hereunder (or where the Company does not have at least three (3) business days advance notice that a Person may become a Successor, within one (1) business day after having notice that such Person may become or has become a Successor). "Person" has the same meaning as such term has for purposes of Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended and as the same may be amended from time to time (the "1934 Act"). "Successor" means any Person that succeeds to, or has the practical ability to control (either immediately or with the passage of time), the Company's business directly, by merger or consolidation, or indirectly, by purchase of the Company's voting securities or all or substantially all of its assets; or

J. any purported termination of Executive's employment which is not in accordance with the terms of this Agreement.

Notwithstanding anything herein to the contrary, at the election of Executive, beginning one hundred eighty-one (181) days following a Change in Control and continuing through the first anniversary of such Change in Control, Executive may terminate his employment upon thirty (30) days written notice for any reason or no reason and such termination will be treated as having occurred for Good Reason.

(f) Change of Control. A "Change in Control" of the Company, means the occurrence of any of the following events:

(i) any Person (except (A) the Company or any affiliate of the

Company, or (B) any Employee Benefit Plan (or any trust forming a part thereof) maintained by the Company or any Subsidiary of the Company) is or becomes the beneficial owner, directly or indirectly, of the Company's securities representing 30.0% or more of the combined voting power of the Company's then outstanding securities, other than pursuant to a transaction described in clause (iii). "Subsidiary" means, with respect to any corporation, any business entity of which a majority of its voting power or its equity securities or equity interests is owned, directly or indirectly, by such corporation;

(ii) there occurs a sale, exchange, transfer or other disposition of substantially all of the assets of the Company to another entity, except to an entity controlled directly or indirectly by the Company;

(iii) there occurs a merger, consolidation, share exchange, tender offer, division or other reorganization of or relating to the Company, unless

A. the shareholders of the Company immediately before such merger, consolidation, share exchange, division or reorganization own, directly or indirectly, immediately thereafter at least 66-2/3% of the combined voting power of the outstanding voting securities of the Surviving Company (as defined below) in substantially the same proportion as their ownership of the voting securities immediately before such merger, consolidation, share exchange, division or reorganization; and

B. the individuals who, immediately before such merger, consolidation, share exchange, division or reorganization, are members of the Incumbent Board (as defined below) continue to constitute at least two-thirds of the board of directors of the Surviving Company; provided, however, that if the election, or nomination for election by the Company's shareholders, of any new director was approved by a vote of at least two-thirds of the

Incumbent Board, such director shall, for the purposes hereof, be considered a member of the Incumbent Board; and provided further, however, that no individual shall be considered a member of the Incumbent Board if such individual initially assumed office as a result of either an actual or threatened Election Contest or Proxy Contest (as both such terms are defined below), including by reason of any agreement intended to avoid or settle any Election Contest or Proxy Contest; and

C. no Person (except (x) the Company or any Subsidiary of the Company, (y) any Employee Benefit Plan (or any trust forming a part thereof) maintained by the Company or any Subsidiary of the Company, or (z) the Surviving Company or any Subsidiary of the Surviving Company) has beneficial ownership of 30.0% or more of the combined voting power of the Surviving Company's outstanding voting securities immediately following such merger, consolidation, share exchange, tender offer, division or reorganization. "Surviving Company" means the business entity that is a resulting company following a merger, consolidation, share exchange, division or other reorganization of or relating to the Company. "Incumbent Board" means the Board of Directors of the Company as constituted at any relevant time. "Election Contest" means a solicitation with respect to the election or removal of directors that is subject to the provisions of Rule 14a-11 of the 1934 Act. "Proxy Contest" means the solicitation of proxies or consents by or on behalf of a Person other than the Board of Directors;

(iv) a plan of liquidation or dissolution of the Company, other than pursuant to bankruptcy or insolvency laws, is adopted; or

(v) during any period of two consecutive years, individuals who, at the beginning of such period, constituted the Board of Directors cease for any reason to constitute at least a majority of the Board of Directors, unless the election, or the nomination for election by

the Company's shareholders, of each new director was approved by a vote of at least two-thirds of the directors then still in office who were directors at the beginning of the period; provided, however, that no individual shall be considered a member of the Board of Directors at the beginning of such period if such individual initially assumed office as a result of either an actual or threatened Election Contest or Proxy Contest, including by reason of any agreement intended to avoid or settle any Election Contest or Proxy Contest.

Notwithstanding the foregoing, a Change in Control shall not be deemed to have occurred if a Person becomes the beneficial owner, directly or indirectly, of securities representing 30.0% or more of the combined voting power of the Company's then outstanding securities solely as a result of an acquisition by the Company of its voting securities which, by reducing the number of shares outstanding, increases the proportionate number of shares beneficially owned by such Person; provided, however, that if a Person becomes a beneficial owner of 30.0% or more of the combined voting power of the Company's then outstanding securities by reason of share repurchases by the Company and thereafter becomes the beneficial owner, directly or indirectly, of any additional voting securities of the Company, then a Change in Control shall be deemed to have occurred with respect to such Person under clause (i).

Notwithstanding anything contained herein to the contrary, if the Executive's employment is terminated and he reasonably demonstrates that such termination (x) was at the request of a third party who has indicated an intention of taking steps reasonably calculated to effect a Change in Control and who effects a Change in Control, or (y) otherwise occurred in connection with, or in anticipation of, a Change in Control which actually occurs, then for all purposes hereof, a Change in Control shall be deemed to have occurred on the day immediately prior to the date of the termination of Executive's employment.

5. Compensation and Benefits Upon Termination.

(a) If Executive's employment is terminated for Good Reason, without Cause or by reason of Disability:

(i) Base Salary and Payment Schedule. The Company shall, for a period of twenty-four (24) months from the date of termination, pay to Executive the highest Base Salary paid during the period including the year in which such termination occurs and the preceding two (2) years, in accordance with the normal payroll policies of the Company. Executive shall also be entitled to a payment ("Vacation Payment") attributable to Base Salary for unused vacation accrued. Such Vacation Payment shall be made to Executive in a lump sum within thirty-days (30) following the date of Executive's termination of employment.

(ii) Bonus. The Company shall, for a period of twenty-four (24) months from the date of termination, pay Executive an amount equal to the highest bonus payment made to Executive during the preceding two (2) years pursuant to any Company incentive bonus plan.

(iii) Contribution Plans. The Company shall, for a period of twenty-four months from the date of termination, pay Executive an amount equal to the highest amounts contributed to all Company tax qualified and non-qualified contribution plans (other than Executive's own contributions) in the year of Executive's termination of employment or the proceeding two (2) years;

(iv) Medical Benefits. Executive will be eligible to:

(v) elect individual and dependent continuation group health and (if applicable) dental coverage, as provided under Section 4980B(f) of the Internal Revenue Code ("COBRA"), for the maximum COBRA coverage period available, subject to all conditions and

limitations (including payment of premiums and cancellation of coverage upon obtaining duplicate coverage or Medicare entitlement). If Executive or one or more of Executive's covered dependents elects COBRA coverage, then the Company shall pay the cost of the COBRA coverage for a period of twenty-four (24) months from the date of termination; or

(vi) receive payments from the Company in equal amounts to payments the Company would have to make pursuant to 5(a)(iii)(A) above.

(vii) Benefit Plans. Executive shall continue to accrue additional benefits under any Company tax-qualified or non-tax qualified defined benefit plan (each a "Defined Benefit Plan") for period of twenty-four months from the date of termination based on the highest compensation paid to Executive in the year of Executive's termination of employment or the proceeding two (2) years. Any payments due to Executive pursuant to this Section 5(a)(v) shall be made in accordance with the applicable Defined Benefit Plan.

(viii) Offset. If such termination is due to Disability, the Company shall have the right to offset any payments made to Executive pursuant to this Section 5(a) by any amounts paid to Executive pursuant to any Company disability plan.

(ix) Disability Benefits. If such termination is due to Disability, Executive shall be eligible to:

(x) elect to continue to receive all disability benefits pursuant to any Company disability plan for the remaining term of this Agreement. If Executive elects to continue to receive disability benefits, then the Company shall pay all costs related to Executive's continued participation in the disability plan; or

(xi) receive tax-effected payments from the Company in equal amounts to payments the Company would have to make pursuant to 5(a)(vii)(A) above.

(b) If Executive's employment is terminated by reason of Death:

(i) Base Salary and Payment Schedule. The Company shall for one (1) year pay to Executive's legal representative the highest Base Salary paid during the period including the year in which such termination occurs and the preceding two (2) years, in accordance with the normal payroll policies of the Company;

(ii) Bonus. The Company shall for one (1) year, pay Executive's legal representative an amount equal to the highest payment made to Executive during the preceding two (2) years pursuant to any Company incentive bonus plan.

(iii) Contribution Plans. The Company shall for one (1) year, pay Executive's legal representative an annual amount equal to the highest amounts contributed to all tax qualified and non-qualified contribution plans (other than Executive's own contributions) in the year of Executive's termination of employment or the proceeding two (2) years;

(iv) Medical Benefits. Executive's covered dependants will be eligible to:

(v) elect individual and dependent continuation group health and (if applicable) dental coverage, as provided under Section 4980B(f) of the Internal Revenue Code ("COBRA"), for the maximum COBRA coverage period available, subject to all conditions and limitations (including payment of premiums and cancellation of coverage upon obtaining duplicate coverage or Medicare entitlement). If Executive's covered dependents elect COBRA coverage, then the Company shall pay the cost of the COBRA coverage for a period of twenty-four (24) months from the date of termination. Executive's covered dependents shall be responsible for paying the full cost of the COBRA coverage (including the administrative charge) after the earlier of (x) a term of one (1) year; or (y) eligibility for coverage under another

employer's medical plan; or

(vi) receive payments from the Company in equal amounts to payments the Company would have to make pursuant to 5(b)(iv)(A) above.

(vii) Benefit Plans. Executive shall continue to accrue additional benefits under any Company tax-qualified or non-tax qualified defined benefit plan (each, a "Defined Benefit Plan") for one (1) year based on the highest compensation paid to Executive in the year of Executive's termination of employment or the proceeding two (2) years. Any payments due to Executive's legal representative pursuant to this Section 5(b)(v) shall be made in accordance with the applicable Defined Benefit Plan.

(c) If Executive's employment is terminated by Executive without Good Reason or by the Company for Cause, the Company will pay to Executive all Base Salary, at the rate then in effect, accrued through the date of Executive's termination of active employment and Executive shall also be entitled to a Vacation Payment attributable to Base Salary for unused vacation accrued. Such Vacation Payment shall be made to Executive in a lump sum within thirty-days (30) following the date of Executive's termination of employment.

6. Funding of Termination Compensation and Benefits. If this Agreement is terminated (a) by the Company without Cause or by the Executive for Good Reason and (b) a Change in Control has occurred, Executive may require that (x) all compensation and benefits payable to Executive pursuant to Section 5 shall be secured through a grantor trust, letter of credit, or similar arrangement and (y) that the present value of certain compensation (including, without limitation, Base Salary, Bonus and Vacation Payment) payments shall be paid to Executive in one lump sum payment.

7. Gross-Up. If there is a change in control of the Company (within the meaning of Section 280G of the Internal Revenue Code of 1986, as amended (the "Code")), the Company shall be required to pay (the "Gross-Up Payment") to Executive or on his behalf any excise taxes imposed on any payments and benefits paid to Executive pursuant to Section 5 hereof. The Company shall also pay any additional income tax liability imposed on Executive as a result of the Gross-Up Payment.

8. Offset for Severance Pay. The Company shall have the right to offset any payments and benefits made to Executive pursuant to Section 5 by any payments made to Executive pursuant to any severance agreement or policy.

9. No Mitigation. Upon termination of Executive's employment (i) without Cause, (ii) for Good Reason, or (iii) in any case after a Change in Control, Executive shall not be required to mitigate damages with respect to the amount of any payment provided under this Agreement by seeking other employment or otherwise, nor shall the amount of any payment provided under this Agreement be reduced by retirement benefits, deferred compensation or any compensation earned by Executive as a result of employment by another employer.

10. D&O Insurance. The Company shall provide Executive with commercially reasonable director and officer liability insurance at all times during the term of this Agreement (including any renewal term), and for a period of six (6) years following the expiration or termination of this Agreement.

11. Confidentiality/Settlement of Existing Rights.

(a) In order to induce Executive to enter into this Agreement, and in order to enable Executive to provide services on behalf of the Company, during the term of this Agreement, the Company will provide Executive with access to certain trade secrets and

confidential or proprietary information belonging to the Company, which may include, but is not limited to, the identities, customs, and preferences of the Company's existing and prospective clients, customers, tenants or vendors; the identities and skills of the Company's employees; the Company's methods, procedures, analytical techniques, and models used in providing products and services, and in pricing or estimating the cost of such products and services; the Company's financial data, business and marketing plans, projections and strategies; customer lists and data; tenant lists and data, vendor lists and data; training manuals, policy manuals, and quality control manuals; software programs and information systems; and other information relating to the development, marketing, and provision of the Company's products, services, and systems (i.e., "Confidential Information"). Executive acknowledges that this Confidential Information constitutes valuable, special and unique property of the Company.

(b) Executive agrees that, except as may be necessary in the ordinary course of performing his duties under this Agreement, Executive shall not, without prior express written consent of the Company (i) use such Confidential Information for Executive's own benefit or for the benefit of another; or (ii) disclose, directly or indirectly, such Confidential Information to any person, firm, corporation, partnership, association, or other entity (except for authorized personnel of the Company) at any time prior or subsequent to the termination or expiration of this Agreement.

(c) By this Agreement, the Company is providing Executive with rights that Executive did not previously have. In exchange for the foregoing and the additional terms agreed to in this Agreement, Executive agrees that all Company Proprietary and Confidential Information learned or developed by Executive during past employment with the Company and all goodwill developed with the Company's clients, customers and other business contacts by

Executive during past employment with the Company is now the exclusive property of the Company, and will be used only for the benefit of the Company, whether previously so agreed or not. Executive expressly waives and releases any claim or allegation that he should be able to use client and customer goodwill, specialized Company training, or Confidential Information, that was previously received or developed by Executive while working for the Company for the benefit of any competing person or entity.

12. Return of Company Property. Executive acknowledges that all memoranda, notes, correspondence, databases, discs, records, reports, manuals, books, papers, letters, CD ROMs, keys, passwords and access codes, client/customer/vendor/supplier profile data, contracts, orders, and lists, software programs, information and records, and other documentation (whether in draft or final form) relating to the Company's business, and any and all other documents containing Confidential Information furnished to Executive by any representative of the Company or otherwise acquired or developed by him in connection with his association with the Company (collectively, "Recipient Materials") shall at all times be the property of the Company. Within seventy-two (72) hours of the termination of his relationship with the Company, Executive promises to return to the Company any Recipient Materials that are in his possession, custody or control, regardless of whether such Materials are located in Executive's office, automobile, or home or on Executive's business or personal computers. Executive also shall authorize and permit the Company to inspect all computer drives used or maintained by Executive during his employment or consulting at the Company and, if necessary, to permit the Company to delete any Recipient Materials or Proprietary Information contained on such drives.

13. Protective Covenants. Executive agrees that the following covenants are reasonable and necessary agreements for the protection of the business interests covered in the fully enforceable, ancillary agreements set forth in this Agreement:

(a) No Interference with Client/Customer Relationships. Executive agrees that, for one year after Executive's employment with the Company ceases, Executive will not induce or attempt to induce any client or customer of the Company to diminish, curtail, divert, or cancel its business relationship with the Company. This paragraph is geographically limited to a fifty-mile (50) radius of Southampton, Pennsylvania.

(b) No Unfair Competition. Executive agrees that for one year after Executive's employment with the Company ceases, Executive will not participate in, work for, or assist a Competing Business in any capacity (as owner, employee, consultant, contractor, officer, director, lender, investor, agent, or otherwise), unless given the prior written consent of the Board to do so. This restriction is limited to a fifty-mile (50) radius of Southampton, Pennsylvania. Nothing herein will prohibit ownership of less than 5% of the publicly traded capital stock of a corporation so long as this is not a controlling interest, or ownership of mutual fund investments.

(c) Remedies. In the event of breach or threatened breach by Executive of any provision of Section 11, 12 or 13 hereof, the Company shall be entitled to (i) injunctive relief by temporary restraining order, temporary injunction, and/or permanent injunction; (ii) recovery of all attorneys' fees and costs incurred by the Company in obtaining such relief; and (iii) any other legal and equitable relief to which may be entitled, including, without limitation, any and all monetary damages that the Company may incur as a result of said breach or threatened breach, in each case without the necessity of posting any bond. The Company may pursue any

remedy available, including declaratory relief, concurrently or consecutively in any order as to any breach, violation, or threatened breach or violation, and the pursuit of one such remedy at any time will not be deemed an election of remedies or waiver of the right to pursue any other remedy.

14. Arbitration. If any dispute shall arise between any of the parties hereto with reference to the interpretation of this Agreement or their rights with respect to any transaction involved, the dispute shall be settled solely and exclusively through arbitration in accordance with the rules of the American Arbitration Association; provided, however, that Company shall remain entitled to all remedies under Section 13(c).

15. Merger or Acquisition; Disposition and Assignment. In the event the Company should consolidate, or merge into another entity, or transfer all or substantially all of its assets or operations to another Person, or divide its assets or operations among a number of entities, this Agreement shall continue in full force and effect with regard to the surviving entity and may be assigned by the Company if necessary to achieve this purpose. Executive's obligations under this Agreement are personal in nature and may not be assigned by Executive to another Person.

16. Payment of Fees and Expenses Relating to Agreement. The Company shall reimburse Executive for all fees and expenses incurred in connection with enforcing this Agreement (including without limitation, attorneys' fees).

17. Notices. All notices, requests, consents, and other communications under this Agreement shall be in writing and shall be deemed to have been delivered on the date personally delivered or on the date deposited in a receptacle maintained by the United States Postal Service for such purpose, postage prepaid, by certified mail, return receipt requested, or by express mail or overnight courier, addressed to the address indicated under the signature block for that party

provided below. Either party may designate a different address by providing written notice of a new address to the other party.

18. Severability. If any provision contained in this Agreement is determined to be void, illegal or unenforceable by a court of competent jurisdiction, in whole or in part, then the other provisions contained herein shall remain in full force and effect as if the provision that was determined to be void, illegal, or unenforceable had not been contained herein. In making any such determination, the determining court shall deem any such provision to be modified so as to give it the maximum effect permitted by applicable law.

19. Waiver, Construction and Modification. The waiver by any party hereto of a breach of any provision of this Agreement shall not operate or be construed as a waiver of any subsequent breach by any party. This Agreement may not be modified, altered or amended except by written agreement of all the parties hereto.

20. Governing Law and Venue. It is the intention of the parties that the laws of the Commonwealth of Pennsylvania should govern the validity of this Agreement, the construction of its terms, and the interpretation of the rights and duties of the parties hereto without regard to any contrary conflicts of laws principles. The agreed upon venue and personal jurisdiction for the parties on any claims or disputes under this Agreement is Bucks County, Pennsylvania.

21. Representation of Executive. Executive hereby represents and warrants to the Company that Executive has not previously assumed any obligations that would prevent him from accepting, retaining and/or engaging in full employment with the Company, or which Executive could violate in the ordinary course of his duties for the Company. Further, Executive hereby represents and warrants to the Company that Executive has not previously assumed any obligations that are inconsistent with those contained in this Agreement, and that he will not use,

disclose, or otherwise rely upon any confidential information or trade secrets derived from any previous employment, if Executive has any, in the performance of his duties on behalf of the Company. Further, Executive acknowledges that he has read and is fully familiar with the terms of this Agreement, has had a reasonable opportunity to consider this Agreement and to seek legal counsel, and after such review, Executive stipulates that the promises made by him in this Agreement are not greater than necessary for the protection of the Company's good will and other legitimate business interests and do not create undue hardship for Executive or the public.

22. Complete Agreement. This Agreement contains the complete agreement and understanding concerning the employment arrangement between the parties and will supersede all other agreements, understandings or commitments between the parties as to such subject matter. The parties agree that neither of them has made any representations concerning the subject matter of this Agreement except such representations as are specifically set forth herein. The parties agree that, except as specifically contemplated by this Agreement, this Agreement supersedes any other agreement, plan or arrangement that may now exist that may otherwise apply to or include Executive regarding employment, compensation, bonus, severance or retention benefits, that any such agreements, plans or arrangements are hereby terminated with respect to Executive and that none of the Company nor any affiliate of the Company will have any liability or obligation to Executive, his heirs, successors or beneficiaries with respect to the existence or termination of any such agreements, plans or arrangements, notwithstanding the terms of any of them.

23. Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of the Company, its successors, legal representatives and assigns, and upon Executive, his heirs, executors, administrators, representatives and assigns. It is specifically agreed that

upon the occurrence of any of the events specified in Section 15 above, the provisions of this Agreement shall be binding upon and inure to the benefit of and be assumed by any surviving or resulting Person or any such Person to which such assets shall be transferred.

24. Captions. The Section and other headings used in this Agreement are for the convenience of the parties only, are not substantive and shall not affect the meaning or interpretation of any provision of this Agreement.

25. Counterparts. This Agreement may be signed in counterparts, which together shall constitute one and the same agreement.

IN WITNESS WHEREOF, and intending to be legally bound, the parties agree to each of the foregoing terms.

EXECUTIVE:

By: ______________________________

Duane D. Deaner

707 Crestbrook Avenue

Cherry Hill, NJ 08003

THE COMPANY:

ENVIRONMENTAL TECTONICS CORPORATION

By: ______________________________

Name: William F. Mitchell

Title: President

Address: Environmental Tectonics Corporation
County Line Industrial Park
Southampton, Pennsylvania 18966

Exhibit A to Deaner Employment Agreement

Base Annual Salary: $97,469.00

Exhibit B to Deaner Employment Agreement

Key Management Bonus Plan

EXHIBIT 10.34

H. F. Lenfest
Five Tower Bridge
300 Barr Harbor Drive, Suite 460
Conshohocken, PA 19428

May 9, 2007

William F. Mitchell
Chief Executive Officer
Environmental Tectonics Corporation
County Line Industrial Park
Southampton, PA 18966

Re: Commitment to Support Environmental Tectonics Corporation

Dear Bill:

In accordance with recent discussions with you and the Board of Directors, subject to an agreement on normal and customary mutually acceptable terms, I commit to provide my personal guarantee of the financial obligations undertaken by Environmental Tectonics Corporation ("ETC" or the "Company") in connection with a credit facility (the "Proposed Credit Facility") of $15 million which ETC intends to enter into with an institutional lender. Upon execution of the Proposed Credit Facility, my existing personal guarantee of the $5 million letter of credit facility from PNC Bank would be terminated. ETC's $15 million equity line, on which you have drawn down $6 million and issued me 6,000 shares of preferred stock, and which ends on October 6, 2007, would also be terminated, as would ETC's Unsecured $3 million Promissory Note (the "Note") which also ends on October 6, 2007. The $6 million preferred stock investment would stay in place, but the $2 million currently due under the Note would be repaid at settlement.

If ETC is unable to reach agreement with an institutional lender on acceptable terms for the Proposed Credit Facility, I agree: (i) to maintain my personal guarantee of the $5 million letter of credit facility from PNC Bank through June 30, 2008; (ii) to fund all requests for advances made in accordance with the terms of the existing $3 million Note; (iii) to fund all requests for draw downs made in accordance with the terms of the existing $15 million equity credit line; and, if for any reason funds are not available under these existing agreements, (iv) to fund all requests by ETC for funds to support its operations through June 30, 2008, on terms and normal and customary conditions to be mutually agreed upon by me and ETC, provided that ETC shall not request more than an additional $10 million in the aggregate from the date of this letter through June 30, 2008 (including all requests made under the existing $3 million Note and $15 million equity credit line).

I also agree to defer the payment of interest under the existing subordinated note and the payment of dividends under the existing $15 million equity credit line until at least June 30, 2008.

At my request at any time between the date of this letter and November 9, 2008, ETC agrees to use its best efforts to make a public offering of ETC's securities, which offering shall be made in compliance with all rules and regulations of the Securities and Exchange Commission and the American Stock Exchange. ETC's objective with such public offering will be to replace any financing commitments then currently in place which are under my guarantee. However, in any case, I commit to provide ETC with continuous access to funds, in some form, through June 30, 2008, subject to the limitations and conditions set forth in the second paragraph above.

Very truly yours,

/s/ H. F. Lenfest
H. F. Lenfest

cc: Grant Thornton LLP