ENVIRONMENTAL
TECTONICS
CORPORATION

ANNUAL REPORT

QUALITY THROUGH
INTEGRITY AND TECHNOLOGY

BOARD OF DIRECTORS

William F. Mitchell, Chairman (1969)

H.F. Lenfest (2003)

George K. Anderson, M.D. (2003)

George A. Sawyer (2009)

Winston E. Scott (2010)

Linda J. Brent Ed.D (2010)

Roger Colley (2011)

Michael D. Malone (2012)

CORPORATE OFFICERS

William F. Mitchell
President and Chief Executive Officer

Thomas G. Loughlin
Chief Operating Officer

Robert L. Laurent, Jr.
Chief Financial Officer

James D. Cashel
General Counsel,
Corporate Secretary

William F. Mitchell, Jr.
Vice President,
Contracts / Purchasing

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TRANSFER AGENT

American Stock Transfer,
New York, New York

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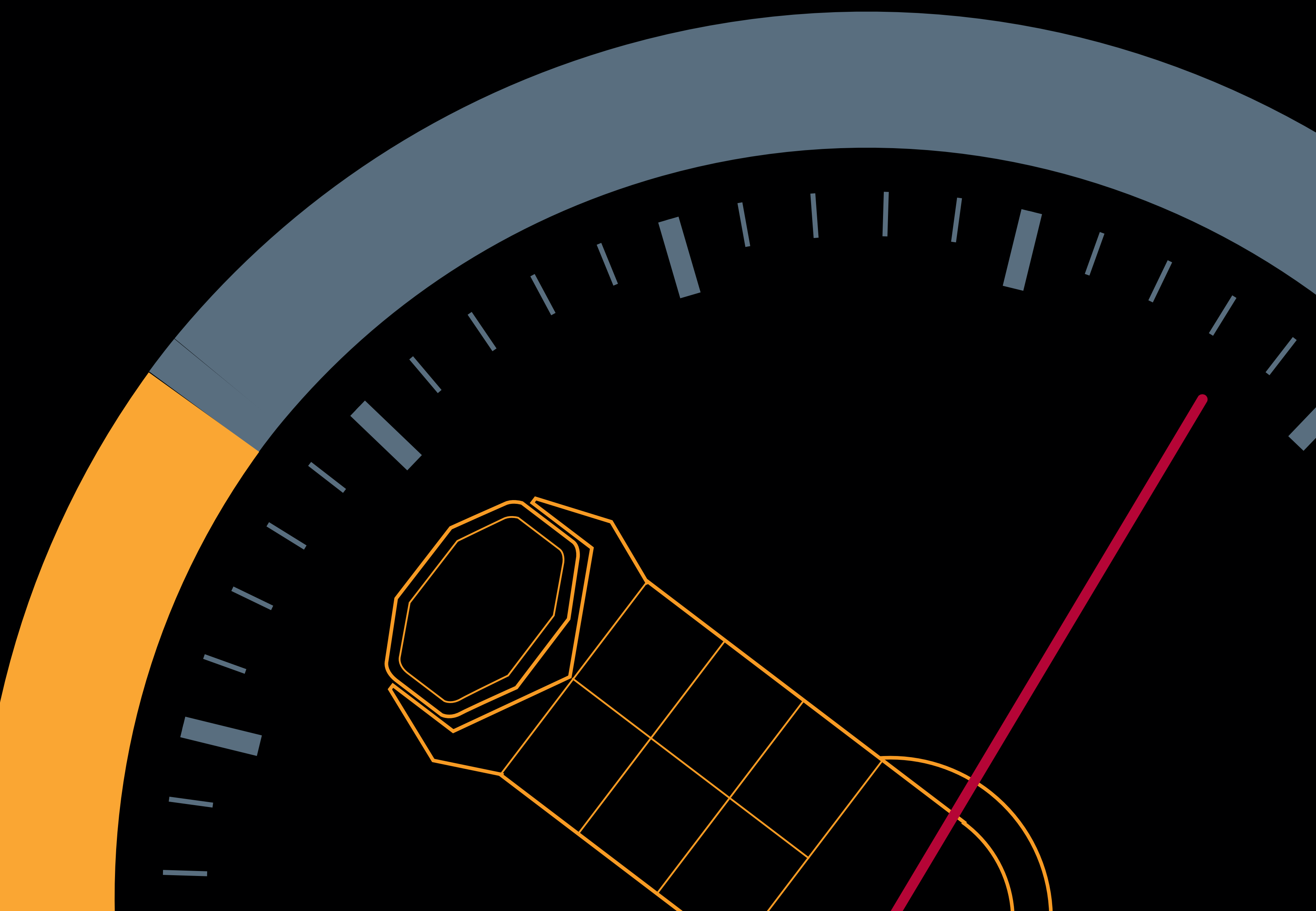


A LETTER FROM OUR PRESIDENT

WE ARE PLEASED TO REPORT THAT ETC HAD ANOTHER STRONG YEAR IN FISCAL 2013. WE CONTINUED TO INNOVATE AND ACHIEVED RECORD PRE-TAX INCOME AND EBITDA. WE BELIEVE THAT ETC IS WELL POSITIONED FOR FUTURE GROWTH.

FINANCIAL HIGHLIGHTS:

- During fiscal 2013, ETC's pre-tax income increased 18% to $8.8 million, while income attributable to our common and participating shareholders increased 29% to $3.4 million on net sales of $62.8 million, which declined approximately 5% from fiscal 2012.

- Diluted earnings per share increased 46% to $0.19 in fiscal 2013 from $0.13 in fiscal 2012.

- EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization) increased approximately 17% to a record $11.7 million in fiscal 2013 compared to $10.0 million in fiscal 2012.

2013 HIGHLIGHTS

In October, we received the final acceptance of a state-of-the-art Aviation Research and Training Center supplied to the Republic of Korea Air Force (RoKAF). The Center sets the benchmark of excellence in Aerospace Medical Training and Research and is equipped with seven man rated training systems: the Authentic Tactical Fighting System ("ATFS") high performance human centrifuge; a state-of-the-art Ejection Seat Simulator with aircraft simulation capability and a visual display system; two Advanced Spatial Disorientation Trainers, a Hypobaric (altitude) chamber with pressure suit training capability; a Night Vision and Night Vision Goggle Training System, and a hyperbaric (dive) chamber. The new center will be used to train RoKAF aircrews in the areas of high-G tolerance, tactical flight maneuvers, hypoxia, spatial disorientation, upset recovery, night vision and night vision goggle operations, and ejection procedures in the highest fidelity and most technologically advanced equipment anywhere.

In a letter of appreciation presented to ETC during final acceptance, the RoKAF states the award was given "in recognition of your high interest and tremendous contribution to the enhancement of the RoKAF forces, in particular for your active effort and support in the timely acquisition of Airborne Crew Flight Environment Adaptation Equipment."

Also in October, ETC was awarded a contract to provide the Spanish Air Force with an altitude (hypobaric) chamber Model 12/4, logistics support, and relocation and recertification of their existing ETC-built hypobaric chamber for a total contract value of $6 million. The new and relocated chambers will be installed in a new aeromedical facility that is being constructed at Torrejon Air Base in Madrid, Spain.

In April, we were awarded an upgrade contract to modernize an aeromedical center in eastern Europe. The contract is valued at more than $9.3 million, and will include a total upgrade of the existing aeromedical training facility.

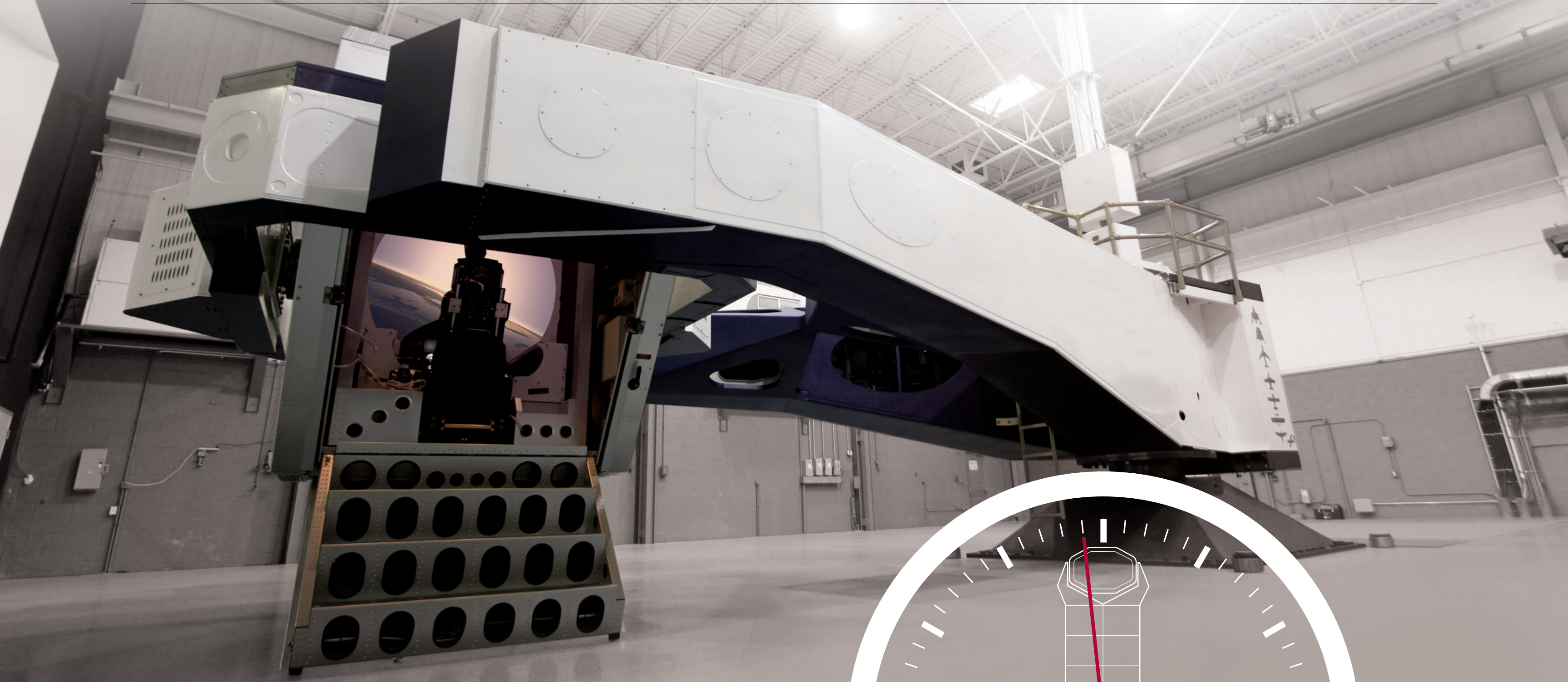
Our Sterilization Systems business unit recognized record sales of nearly $11 million in fiscal 2013 on strong orders, while our Environmental Testing and Simulation business unit also recognized solid growth.

FINANCIAL RESTRUCTURING

In September, we completed a financial restructuring that reduces our annual net cash payments for dividends and interest by approximately $1.5 million per year. The financial restructuring also reduced the number of participating preferred shares in the amount equivalent to 5 million shares of Common Stock, or nearly 25% of the total outstanding common and participating shares. Following the restructuring, the dividends on the remaining Series E Preferred Stock were reduced from ten percent to four percent.

You may have noticed that earlier this year the Company filed papers with the Securities and Exchange Commission ("SEC") to voluntarily deregister our Common Stock – or to "go dark". Our decision to "go dark" was made in large part because of our size and market capitalization, and the high costs and demands on senior management's time to comply with SEC and Sarbanes-Oxley reporting requirements. In addition to allowing senior management to devote more resources to ETC's core businesses, we expect to recognize substantial cost savings, such as lower professional fees, associated with this decision. Rest assured that we intend to continue to prepare and publish quarterly and annual financial results that will include much of the financial information currently disclosed in the Company's periodic SEC reports, and our annual financial statements will continue to be certified by an independent auditor.

OUR INCREASED EARNINGS AND INCREASED CASH FLOW RESULTED FROM HIGHER PROFITABILITY ON A STRONG PRODUCT AND CUSTOMER MIX, LOWER OPERATING EXPENSES AND THE POSITIVE EFFECT FROM A SEPTEMBER 2012 FINANCIAL RESTRUCTURING.



OUR TIME APPROACHES

THE YEARS AHEAD HOLD ENORMOUS PROMISE FOR ETC. In the area of tactical flight simulation, I am pleased to report that in January 2013, the U.S. Congress included a provision in the recently-passed National Defense Authorization Act that requires an independent study on the implications of simulator-based training for fighter aircraft in a sustained gravity environment. We are pleased that Congress is embarking on this study and are optimistic the study will reveal what we support: that sustained gravity tactical flight simulators, like ETC's ATFS Motion Platforms, provide a viable, highly advantageous alternative to live aircraft for tactical flight training purposes that would significantly reduce fighter aircraft training costs. ETC is uniquely positioned to deliver this simulator-based training, and the full acceptance of it by the U.S. Department of Defense would be a tremendous business opportunity for ETC.

As predicting the unpredictable becomes more nuanced than ever, ETC is making sure our customers meet the future prepared. ETC stands out as distinctively able to keep moving toward the future and to keep generating value for our customers around the world. And that, in turn, promises to continue generating value for our shareholders.

Let me close by expressing my pride in the worldwide ETC team for bringing us to this point, and my gratitude to you, our shareholders, for your unwavering support. I trust you share in our excitement about your company's performance and the way in which ETC's talented workforce is building on our storied past to chart a course to an even brighter future.

Wm F Mitchell

William F. Mitchell
President and Chief Executive Officer
Environmental Tectonics Corporation (ETC)

FINANCIAL REVIEW

(in thousands, except per share information)	Fiscal year ended February 22, 2013		Fiscal year ended February 24, 2012	
Net sales	$	62,773	$	66,294
Gross profit		24,869		23,531
Operating income		9,944		8,137
Net income attributable to Environmental Tectonics Corporation		4,948		4,873
Per share information:				
Basic earnings per common and participating share:				
Distributed earnings per share:				
Common	$	-	$	-
Preferred	$	0.17	$	0.20
Undistributed earnings per share:				
Common	$	0.19	$	0.13
Preferred	$	0.19	$	0.13
Diluted earnings per share	$	0.19	$	0.13
Working capital	$	25,135	$	27,786
Total long-term debt obligations		22,185		16,724
Total assets		60,568		67,786
Total shareholders' equity		24,219		30,825
Weighted average common and participating shares:				
Basic		18,212		20,209
Diluted		18,375		20,497

When used in this Annual Report to Shareholders, except where the context otherwise requires, the terms “we”, “us”, “our”, “ETC”, and the “Company” refer to Environmental Tectonics Corporation and its subsidiaries.

We have never paid any cash dividends on our Common Stock and do not anticipate that any cash dividends will be declared or paid on our Common Stock in the foreseeable future.

Dividends on the Company’s Preferred Stock, as declared, are accrued according to the terms of the Preferred Stock and are paid in cash. All Preferred Stock dividends accrued as of February 22, 2013 were paid in April 2013.

MANAGEMENT'S DISCUSSION AND ANALYSIS

FORWARD-LOOKING STATEMENTS

Discussions of some of the matters contained in this Annual Report to Shareholders include forward-looking statements that may involve risks and uncertainties. Some of these discussions are contained under the caption "Management's Discussion and Analysis". We have based these forward-looking statements on our current expectations and projections about future events or future financial performance, which include implementing our business strategy, developing and introducing new technologies, obtaining, maintaining and expanding market acceptance of the technologies we offer, and competition in our markets. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about ETC 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 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 foreign currency fluctuations, (ii) statements of our plans and objectives of the Company or its management or the Company's Board of Directors (the "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, (vi) statements regarding the Company's ability to obtain financing to support its operations and other expenses, and (vii) statements preceded by, followed by, or, that include, terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "future", "predict", "potential", "intend", or "continue", and similar expressions. These forward-looking statements involve risks and uncertainties that 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.

References to fiscal 2012 are references to the fifty-two week period ended February 24, 2012. References to fiscal 2013 are references to the fifty-two week period ended February 22, 2013. References to fiscal 2014 are references to the fifty-three week period ending February 28, 2014.

Overview

ETC was incorporated in 1969 in Pennsylvania. For over four decades, we have provided our customers with products, service, and support. Innovation, continuous technological improvement and enhancement, and product quality are core values that are critical to our success. We are a significant supplier and innovator in the following product areas: (i) software driven products and services used to create and monitor the physiological effects of flight, including high performance jet tactical flight simulation, upset recovery and spatial disorientation, and both suborbital and orbital commercial human spaceflight; collectively, Aircrew Training Systems ("ATS"); (ii) altitude (hypobaric) chambers; (iii) the Advanced Disaster Management Simulator ("ADMS"); (iv) steam and gas (ethylene oxide) sterilizers; (v) environmental testing and simulation devices; and (vi) hyperbaric (100% oxygen) chambers for one person (monoplace chambers). We operate in two primary business segments, Aerospace Solutions ("Aerospace") and Commercial/ Industrial Systems ("CIS").

Aerospace encompasses the design, manufacture, and sale of: (i) Aircrew Training Systems; (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); and (iv) ADMS, as well as integrated logistics support for customers who purchase these products or similar products manufactured by other parties. These products and services provide customers with an offering of comprehensive solutions for improved readiness and reduced operational costs. Sales of our Aerospace products are made principally to U.S. and foreign government agencies.

Specific products within Aerospace include:

- Authentic Tactical Fighting System ("ATFS") Motion Platforms;
    - ATFS-400-31 PHOENIX High Performance Human Centrifuge
    - ATFS-400-25 PHOENIX High Performance Human Centrifuge
- Cockpit Modules;
- Turn-Key Aeromedical Centers;
- GYROLAB GL-6000 Gryphon High-G Disorientation Training and Research Device;
- GYROLAB GL-4000;
- GYROLAB GL-2500;
- GYROLAB GL-1500;
- GYRO Integrated Physiological Trainer, Generation 3, Extended Field of View ("GYRO IPT3 EFOV");
- GYRO IPT II;
- GyroFlight;
- HeloFlight;
- GAT II Fixed Wing General Aviation Trainer;
- GAT II Helo;
- G-LAB Motion Platform;
- Integrated Avionics Maintenance Trainer ("IAMT");

• Altitude (Hypobaric) Chambers;
• Multiplace Hyperbaric Chambers;
• Vestibular Illusion Demonstrator (“VID”);
• Ejection Seat Simulator (“ESS”);
• Pilot Selection System;
• Water Survival Training equipment;
• Night Vision Training System (“NVTS”);
• Night Vision Goggle Training System (“NVGTS”);
• Aviation Gymnastics Equipment (“GTEP”); and
• ADMS line of products (ADMS-AIRBASE, ADMS-COMMAND, ADMS-CONTROL, etc.).

Specific services within Aerospace include:

• Tactical flight training;
• Upset recovery and spatial disorientation training;
• Suborbital and orbital commercial human spaceflight training;
• Aeromedical training;
• Advanced flight training;
• Basic flight training;
• Pilot selection;
• Emergency response training; and
• Integrated logistics support.

CIS encompasses the design, manufacture, and sale of:

• Steam and gas (ethylene oxide) sterilizers;
• Environmental testing and simulation devices;
• Hyperbaric (100% oxygen) chambers for one person (monoplace chambers); and
• Parts and service support.

Sales of our CIS products are made principally to the healthcare, pharmaceutical, and automotive industries.

Net sales, operating income, identifiable assets, and other financial information regarding our segments may be found in Note 9 – Business Segment Information.

The Company’s fiscal year is the 52- or 53-week annual accounting period ending the last Friday in February. Both fiscal 2013 and fiscal 2012 are 52-week periods. Certain amounts from prior consolidated financial statements have been reclassified to conform to the presentation in fiscal 2013.

We presently have two operating subsidiaries. ETC-PZL Aerospace Industries Sp. z o.o. (“ETC-PZL”), our 95%-owned subsidiary in Warsaw, Poland, manufactures simulators and provides software to support our domestic products. Environmental Tectonics Corporation (Europe) Limited (“ETC-Europe”), our 99%-owned subsidiary, functions as a sales office in the United Kingdom.

We utilize both employees and independent representatives to market our products and services. At February 22, 2013, approximately fifty-two (52) employees were committed to sales and marketing functions. In addition to our two operating subsidiaries, we have employees stationed in Egypt, Turkey, United Arab Emirates, India, China, Thailand, and Malaysia. In certain countries outside the United States, we have relationships with independent sales representatives and distributors.

We sell 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 Aerospace segment, we offer integrated Aircrew Training Systems to commercial, governmental, and military defense agencies, and training devices to governmental and military defense agencies both in the United States and internationally. We sell our disaster management simulation training and products to fire and emergency training schools, and state and local governments. We also provide integrated logistics support for customers who purchase these products or similar products manufactured by other parties.

In the CIS segment, we sell our sterilizers to pharmaceutical and medical device manufacturers. We sell our environmental testing and simulation devices primarily to commercial automobile manufacturers and heating, ventilation, and air conditioning (“HVAC”) manufacturers. We sell our hyperbaric products (primarily “monoplace” chambers) to hospitals and clinics. We also provide upgrade, maintenance, and repair services for our products and similar products manufactured by other parties.

Significant Impacts and Transactions during Fiscal 2013

The following items had a material impact on our financial performance, cash flow, and financial position during fiscal 2013:

Impact of financial restructuring and Preferred Stock repurchase

On September 28, 2012, the Company announced a financial restructuring agreement (“2012 Financial Restructuring”) that positively impacted the Company’s earnings by reducing future annual net cash payments for dividends and interest by approximately $1.5 million, and reducing the number of participating preferred shares. As part of the 2012 Financial Restructuring, the Company’s revolving line of credit (“Line of Credit”) with PNC Bank, National Association (“PNC Bank”) was reduced from $20.0 million to $15.0 million, with the expiration date extended to October 31, 2015. The interest rate on the Line of Credit remains substantially unchanged.

PNC Bank also provided to the Company a five-year term loan of $15.0 million (the "Term Loan"), which will expire on September 28, 2017. The Company utilized $10.0 million of the proceeds from the Term Loan to repurchase and retire 10,000 shares of ten percent (10%) Preferred Stock, equivalent to 5,032,091 shares of Common Stock. The revolving Line of Credit is no longer guaranteed by H.F. Lenfest ("Mr. Lenfest"), a major shareholder and member of the Board of Directors, and is instead secured by substantially all of the Company's assets. Mr. Lenfest is providing a guarantee on the new $15.0 million Term Loan until March 31, 2015, after which his guarantee will be removed. In addition, dividends on the remaining Preferred Stock were reduced from ten percent (10%) to four percent (4%), subject to shareholder approval at the 2013 Annual Meeting of Shareholders.

Continued production under U.S. Government contracts

The Base Realignment and Closure Act ("BRAC Act") passed in 2005 by Congress mandated base closures and consolidations through all the U.S. defense services. In the past several years, as a result of the BRAC Act, we were awarded three major contracts within our Aerospace segment. Our fiscal 2013 opening backlog of firm orders in the amount of $74.5 million included approximately $39.0 million for three contracts awarded under the BRAC Act. As a result of reduced engineering and production activity as these contracts transition into the installation phase, sales to the U.S. Government decreased by $5.0 million, or 18.3%, during fiscal 2013 compared to fiscal 2012. The Company's sales backlog as of February 22, 2013 was $48.5 million, of which $17.0 million related to BRAC Act contracts. Given the current domestic economic conditions and political environment, it should not be assumed that any additional BRAC Act contracts will be awarded to us.

Market for our CIS products

Our CIS products are sold primarily to domestic commercial accounts. The Hyperbaric (monoplace) chambers business unit experienced an increase in orders during fiscal 2013 to $4.0 million compared to $3.6 million for fiscal 2012. Our Sterilization Systems business unit orders declined to $6.2 million from the record orders of $11.9 million during fiscal 2012. Our Environmental Testing and Simulation business unit received $1.6 million in orders for domestic and international automotive testing units during fiscal 2013 compared to $2.4 million during fiscal 2012. Though orders were down, revenues increased as a result of orders in backlog entering fiscal 2013.

Continued investments to enhance and market worldwide our ATFS and other technologies

During the past two fiscal years, we have spent $3.4 million (including $1.3 million in fiscal 2013) for capital improvements and software development. Most of this investment has been related to enhancement and promotion of our ATS products and related training, and includes both engineering costs to improve the technical abilities of our ATFS line of products and enhance upset recovery training ("URT"). This investment is in addition to several full time employees and consultants whose main responsibilities are to support ATFS business development. Going forward, we expect to continue to invest in new capabilities of our ATFS line of products.

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 financial statements requires the use of judgments and estimates. Our critical accounting policies are described below to provide a better understanding of how we develop our assumptions and judgments about future events and related estimates, and how they can impact our financial statements. A critical accounting estimate is one that requires our most difficult, subjective, or complex estimates and assessments, and is fundamental to our results of operations. We identified our most critical accounting estimates (not in any specific order) to be:

- estimating budget costs for large, multi-year contracts that involve significant engineering and software development;
- percentage-of-completion ("POC") accounting for long-term, construction-type contracts;
- legal reserves and contingencies;
- valuations of long-lived assets, including equipment housed within our National Aerospace Training and Research Center (the "NASTAR Center") and intangible assets such as capitalized software;
- forecasting our effective income tax rate, including our future ability to value and utilize tax credits and to realize the deferred tax assets, and providing for uncertain tax positions; and
- inventory valuation and reserves.

We base our estimates on historical experience, and on various other assumptions we believe to be reasonable according to the current facts and circumstances; the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. We believe the following are the critical accounting policies used in the preparation of our consolidated financial statements, as well as the significant estimates and judgments affecting the application of these policies. This discussion and analysis should be read in conjunction with our consolidated financial statements and related notes included in this report.

We have discussed the development and selection of these critical accounting policies and estimates with the Audit Committee of the Board of Directors, and the Audit Committee has reviewed the disclosure presented below.

Revenue Recognition

We recognize revenue, which is recorded net of any applicable sales tax, using three methods:

On long-term contracts, with a contract value over $250,000 and a minimum completion period of six months, the POC method is applied based on costs incurred from inception to date as a percentage of estimated total costs required to fulfill the contract. This percentage is then multiplied by the total estimated contract value to determine the cumulative amount of revenue to be recognized, from which previously recognized revenue would be subtracted to determine 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 an 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 (i.e. milestone payments) in excess of revenue recognized on uncompleted long-term contracts are reflected as a 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 that 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. Costs related to post shipment obligations, including field installation, warranty, and any additional contracted items are included in the estimated total costs required to fulfill the contract. 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 POC method involves significant estimates, both at inception and throughout the performance period. Some of our long-term contracts contain provisions that require us to pay liquidated damages if we are responsible for the failure to meet specified contractual milestone dates and the applicable customer asserts a claim under these provisions. Management uses its best judgment to estimate not only the cost to perform the work, but also the price we will eventually be paid on such contracts.

For contracts under $250,000, or contracts to be completed in less than six months, and where there are no post-shipment services included in the contract (such as installation and customer acceptance), the completed contract method is applied and revenue is recognized on the date that the finished product is shipped to the customer. Estimated warranty costs for these contracts are accrued and this accrual is adjusted periodically based on actual warranty expenses and the amount and type of products shipped. Revenue derived from 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. There are no post contract expenses associated with these types of contracts.

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.

Inventory

We periodically evaluate our inventory, which affects gross margin, to ensure that it is carried at the lower of cost or net realizable value. Cost includes appropriate overhead. Overhead allocated to inventory cost includes only costs directly related to our manufacturing activities. These include general supervision, utilities, supplies, etc., and depreciation and software amortization expense. Where necessary, provision is made for obsolete, slow-moving, or damaged inventory. This provision represents the difference between the cost of the inventory and its estimated market value, based on the future demand of our products. To the extent that future events affect the salability of inventory, these provisions could vary significantly.

Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes, as well as the valuation of net loss carry forwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the reliability of the related deferred tax asset.

Results of Operations

Because of the nature of our business, 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 2013 versus Fiscal 2012

Summary Table of Results

(in thousands, except per share information)	**Fiscal 2013**	**Fiscal 2012**	**Variance $**	**Variance %**
Net sales:				
Domestic sales	$ 19,049	$ 16,635	$ 2,414	14.5
U.S. Government sales	22,217	27,181	(4,964)	(18.3)
International sales	21,507	22,478	(971)	(4.3)
Net sales total	62,773	66,294	(3,521)	(5.3)
Gross profit	24,869	23,531	1,338	5.7
Gross profit margin %	*39.6%*	*35.5%*	*4.1%*	*11.5%*
Operating expenses:				
Selling and marketing expenses	5,570	5,481	89	1.6
General and administrative expenses	8,186	8,513	(327)	(3.8)
Research and development expenses	1,169	1,400	(231)	(16.5)
Operating expenses total	14,925	15,394	(469)	(3.0)
Operating income	9,944	8,137	1,807	22.2
Operating margin %	*15.8%*	*12.3%*	*3.5%*	*28.5%*
Interest expense, net	1,005	734	271	36.9
Other expense (income), net	118	(85)	203	238.8
Income before income taxes	8,821	7,488	1,333	17.8
Pre-tax income margin %	*14.1%*	*11.3%*	*2.8%*	*24.8%*
Provision for income taxes	3,859	2,620	1,239	47.3
Net income	4,962	4,868	94	1.9
(Income) expense attributable to non-controlling interest	(14)	5	(19)	(380.0)
Net income attributable to ETC	**$ 4,948**	**$ 4,873**	**$ 75**	**1.5**
Per share information:				
Basic earnings per common and participating share:				
Distributed earnings per share:				
Common	$ -	$ -	$ -	
Preferred	$ 0.17	$ 0.20	$ (0.03)	(15.0)
Undistributed earnings per share:				
Common	$ 0.19	$ 0.13	$ 0.06	46.2
Preferred	$ 0.19	$ 0.13	$ 0.06	46.2
Diluted earnings per share	**$ 0.19**	**$ 0.13**	**$ 0.06**	**46.2**

Net income attributable to ETC

Net income attributable to ETC was $5.0 million, or $0.19 per diluted share, in fiscal 2013 versus $4.9 million, or $0.13 per diluted share, in fiscal 2012; an increase in net income of $0.1 million, or 1.5%. Operating income in fiscal 2013 was $9.9 million versus $8.1 million in fiscal 2012, an increase of $1.8 million, or 22.2%. Operating income was favorably affected in dollars by a higher gross profit and was favorably affected as a percentage of net sales by a 3.0% decrease in operating expenses. The significant increase in diluted earnings per share was due in part to increased income and also to reduced shares outstanding following the repurchase of 386 shares of Series D Preferred Stock, representing all of the Company's issued and outstanding shares of Series D Preferred Stock, and 9,614 shares of Series E Preferred Stock, representing a significant portion of the Company's issued and outstanding Series E Preferred Stock.

Net sales

The following schedule presents the Company's net sales (in thousands) by segment, business unit, and geographic area:

	Fiscal 2013				Fiscal 2012			
	Domestic	**U.S. Gov't**	**International**	**Total**	**Domestic**	**U.S. Gov't**	**International**	**Total**
Aerospace Solutions								
ATS	$ 306	$ 9,553	$ 12,249	$ 22,108	$ 592	$ 17,805	$ 13,894	$ 32,291
Chambers	-	12,664	1,680	14,344	-	9,376	1,633	11,009
Simulation (ADMS)	1,181	-	1,263	2,444	2,032	-	1,184	3,216
ETC-PZL and other	236	-	3,163	3,399	199	-	2,186	2,385
Subtotal	1,723	22,217	18,355	42,295	2,823	27,181	18,897	48,901
Commercial/Industrial Systems								
Sterilizers	9,993	-	901	10,894	6,996	-	57	7,053
Environmental	3,035	-	496	3,531	1,740	-	646	2,386
Hyperbaric	2,220	-	1,643	3,863	2,487	-	2,744	5,231
Service and spares	2,078	-	112	2,190	2,589	-	134	2,723
Subtotal	17,326	-	3,152	20,478	13,812	-	3,581	17,393
Net sales total	**$ 19,049**	**$ 22,217**	**$ 21,507**	**$ 62,773**	**$16,635**	**$ 27,181**	**$ 22,478**	**$ 66,294**

Net sales for fiscal 2013 were $62.8 million, a decrease of $3.5 million, or 5.3%, from fiscal 2012. The decrease is primarily due to lower sales related to major U.S. Government and International contracts that continue to move toward completion, offset in part, by increased sales to Domestic customers.

In fiscal 2013, two customers, (one U.S. defense agency and one international customer), each in the Aerospace segment, represented 10.0% or more of total net sales, and sales to these two customers totaling $29.9 million represented 47.7% of total net sales. In fiscal 2012, three customers, (two U.S. defense agencies and one international customer), each in the Aerospace segment, represented 10.0% or more of total net sales, and sales to these three customers totaling $37.8 million represented 57.0% of total net sales. Within the Company's February 22, 2013 sales backlog of $48.5 million for work to be performed and revenue to be recognized under written agreements after such date, three contracts (two with a U.S. defense agency and one with an international customer), each representing at least 10% of the total sales backlog, together constituted $26.7 million or 55.1% of the total sales backlog. ATS backlog was $12.9 million, or 26.6%, of the total sales backlog; Chambers backlog was $18.8 million, or 38.8%, of the total sales backlog; and Sterilizers backlog was $4.9 million, or 10.0%, of the total sales backlog. ETC-PZL sales backlog totaled $5.5 million, or 11.4% of the total sales backlog as of February 22, 2013.

We have historically experienced significant variability in our sales performance. This reflects the existing sales backlog, product mix, nature of contracts (size and performance time), manufacturing cycle, installation time, customer acceptance, and certain factors not in our control such as customer delays and the time required to obtain U.S. Government export approvals. A small number of contracts may account for a substantial percentage of our net sales in any period.

Domestic sales

Domestic sales in fiscal 2013 were $19.0 million, an increase of $2.4 million, or 14.5%, over fiscal 2012, and represented 30.3% of total net sales, compared to 25.1% in fiscal 2012. The increase in Domestic sales is primarily a result of a $3.0 million, or 42.8%, increase in sales of Sterilization Systems, which reflects record orders received in fiscal 2012, and a $1.3 million, or 74.4%, increase in the sale of Environmental Testing and Simulation Systems. These increases were partially offset by a $0.9 million, or 41.9%, decrease in sales of ADMS as well as smaller decreases in other categories.

U.S. Government sales

U.S. Government sales in fiscal 2013 were $22.2 million, a decrease of $5.0 million, or 18.3%, from fiscal 2012, which reflect lower sales related to a high performance human centrifuge, offset in part, by increased sales related to a suite of altitude (hypobaric) chambers. U.S. Government sales represented 35.4% of total net sales in fiscal 2013 compared with 41.0% in fiscal 2012. Given the existing progress made on U.S. Government contracts in the Company's sales backlog, the Company anticipates the concentration of sales with the U.S. Government will continue to lessen in fiscal 2014.

International sales

International sales in fiscal 2013, including those of the Company's foreign subsidiaries, were $21.5 million, a decrease of $1.0 million, or 4.3%, from fiscal 2012, due primarily to a $1.6 million, or 11.7%, decrease in the sale of ATS products, and a $1.1 million decrease in Hyperbaric sales. These decreases were offset, in part, by a $1.0 million, or 44.7%, increase in ETC-PZL sales as well as smaller increases in other product categories. In aggregate, International sales represented 34.3% of the Company's total net sales, an increase over 33.9% in fiscal 2012. In both fiscal 2013 and fiscal 2012, International sales totaling at least $500,000 were made to customers in eight (8) different countries. 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.

Segment sales

Aerospace sales were $42.3 million in fiscal 2013, a decrease of $6.6 million, or 13.5%, from sales of $48.9 million in fiscal 2012. This decrease was primarily due to less revenue recorded on one of our international contracts for multiple Aerospace products as the aeromedical center in which this equipment is housed was dedicated in October 2012. Sales of these products accounted for 67.4% of our total net sales versus 73.8% in fiscal 2012. Sales in our CIS segment increased $3.1 million, or 17.7%, and constituted 32.6% of our total net sales compared to 26.2% in fiscal 2012.

Given the Company's sales backlog as of February 22, 2013, it is anticipated that our Aerospace segment will begin to generate more of its revenues from International contracts, while sales within our CIS segment are expected to be affected by a lower sales backlog entering fiscal 2014.

Gross profit

Gross profit for fiscal 2013 increased by $1.3 million, or 5.7%, over fiscal 2012. This improvement was achieved despite lower sales due primarily to a more profitable product and customer sales mix. Gross profit margin as a percentage of net sales increased to 39.6% in fiscal 2013 over 35.5% in fiscal 2012. This increase was due primarily to fiscal 2012 costs related to a U.S. government contract, and to a more profitable product and customer sales mix in fiscal 2013.

Selling and marketing expenses

Selling and marketing expenses for fiscal 2013 of $5.6 million increased slightly over fiscal 2012. As a percentage of net sales, selling and marketing expenses increased to 8.9% in fiscal 2013 from 8.3% in fiscal 2012 due primarily to lower net sales in fiscal 2013.

General and administrative expenses

General and administrative expenses for fiscal 2013 of $8.2 million decreased slightly by $0.3 million, or 3.8%, from fiscal 2012. The decrease is primarily the result of lower professional fees and an on-going effort to reduce non-revenue generating expenses. As a percentage of net sales, general and administrative expenses increased to 13.0% in fiscal 2013 compared to 12.8% in fiscal 2012 due primarily to lower net sales in fiscal 2013.

Research and development expenses

Research and development expenses include spending for potential new products and technologies, and work performed internationally under government grant programs. This spending, net of grant payments from the Polish and Turkish governments, totaled $1.2 million for fiscal 2013 compared to $1.4 million in fiscal 2012, a decrease of $0.2 million, or 16.5%. The decrease was a result of more research and development employees being assigned to specific contracts; thus, expenses related to these employees were included in cost of sales in fiscal 2013. Most of the Company's research efforts, which were and continue to be a significant cost of its business, are included in cost of sales for applied research for specific contracts, as well as research for feasibility and technology updates. As a percentage of net sales, research and development expenses decreased slightly to 1.9% in fiscal 2013 compared to 2.1% in fiscal 2012.

Operating income

Operating income increased $1.8 million, or 22.2%, to $9.9 million for fiscal 2013 compared to $8.1 million in fiscal 2012. The 5.7% increase in gross profit combined with a 3.0% reduction in operating expenses generated the increase operating income.

On a segment basis, Aerospace had operating income of $9.1 million for fiscal 2013, a $1.9 million, or 26.7%, increase in operating income compared to $7.2 million in fiscal 2012. CIS had operating income of $3.9 million for fiscal 2013, a $0.2 million, or 4.2%, decrease in operating income compared to $4.1 million in fiscal 2012. These segment operating results were offset, in part, by unallocated corporate expenses.

Given the positive operating performance in fiscal 2013, the level and mix of the Company's sales backlog as of February 22, 2013, open proposals and proposals under preparation, which include quotations for some significant potential international contract awards, and the Company's continuing positive feedback from potential customers for its ATFS technology, it is anticipated that the Company will produce income from operations in fiscal 2014.

Interest expense, net

Interest expense, net for fiscal 2013 was $1.0 million compared to $0.7 million in fiscal 2012, an increase of $0.3 million, or 36.9%. Increased interest expense resulted from a higher level of borrowing following the 2012 Financial Restructuring; however, the cost of this interest expense was more than offset by lower dividends resulting from the 2012 Financial Restructuring, the Preferred Stock Repurchase, and the lowering of Preferred Stock dividends from ten percent (10%) to four percent (4%), reducing our cost of capital.

Other expense (income), net

Other expense, net for fiscal 2013 was $0.1 million compared to other income, net of $0.1 million in fiscal 2012, a decrease of $0.2 million in other income. Other expense (income), net consists primarily of bank and letter of credit fees, as well as foreign currency exchange gains and losses.

Income taxes

As of February 22, 2013, the Company reviewed the components of its deferred tax assets and determined, based upon all available information that its current and expected future operating income will more likely than not result in the realization of its deferred tax assets relating to its federal net operating loss carry forwards. The Company has a net deferred tax asset related primarily to its federal net operating loss carry forwards of $4.8 million. Income tax provisions of $3.9 million were recorded in fiscal 2013 compared to $2.6 million in fiscal 2012 as a result of increased income before income taxes.

Effective tax rates were 43.7% and 35.0% for fiscal 2013 and fiscal 2012, respectively. Our effective fiscal 2013 tax rate was higher than fiscal 2012 primarily due to a smaller reduction in tax expense related to the research and development credit.

As of February 22, 2013, the Company had approximately $13.6 million of federal net loss carry forwards available to offset future income tax liabilities, which begin to expire in 2025. In addition, the Company has the ability to offset deferred tax assets against deferred tax liabilities created for such items as depreciation and amortization.

Liquidity and Capital Resources

On September 28, 2012, the Company announced its 2012 Financial Restructuring, which positively impacted the Company's earnings by reducing future annual net cash payments for dividends and interest by approximately $1.5 million and reduced the number of participating preferred shares. As part of the 2012 Financial Restructuring, the Company's revolving Line of Credit with PNC Bank was reduced from $20.0 million to $15.0 million, with the expiration date extended to October 31, 2015. The interest rate remained substantially unchanged. PNC Bank also provided to the Company a five (5) year $15.0 million Term Loan, which will expire on September 28, 2017. The Company utilized $10.0 million of the proceeds from the Term Loan to repurchase and retire 10,000 shares of ten percent (10%) Preferred Stock, equivalent to 5,032,091 shares of Common Stock. The revolving Line of Credit is no longer guaranteed by Mr. Lenfest, and is instead secured by substantially all of the Company's assets. Mr. Lenfest is providing a guarantee on the new $15.0 million Term Loan until March 31, 2015, after which his guarantee will be removed. In addition, dividends on the remaining Preferred Stock are reduced from ten percent (10%) to four percent (4%), subject to shareholder approval.

On December 19, 2012, the Company entered into an Export Import Loan Agreement through PNC Bank, whereby the Company has an Export Import Committed Line of Credit ("Ex-Im Line of Credit") through which it may borrow against eligible export inventory and eligible export accounts receivable up to a maximum of $2.0 million. The agreement expires on October 31, 2015. Interest on advances under the agreement will be at the PNC Daily LIBOR Rate plus 2.5% (currently 2.70%). The agreement includes covenants that are generally consistent with the Line of Credit with PNC Bank.

As a result of increased net income, and reducing its accounts receivable, offset in part by decreased billings in excess of costs and estimated earnings on uncompleted long-term contracts, the Company was able to generate cash from operations and reduce its borrowing. As of February 22, 2013, the Company's availability under the Line of Credit with PNC Bank was $6.5 million. This reflected cash borrowings of $7.6 million and outstanding letters of credit of approximately $0.9 million. Working capital was $25.1

million and $27.8 million as of February 22, 2013 and February 24, 2012, respectively. The decrease in working capital was primarily the result of the Company reducing its accounts receivable.

With unused availability under the Line of Credit with PNC Bank and the Company's ability to generate cash from operations, the Company anticipates these sources of liquidity will be sufficient to fund its operating activities, anticipated capital expenditures, and debt repayment obligations throughout fiscal 2014.

Cash flows from operating activities

Cash provided by operations is driven by income from the sale of our products, which depends on the timing of receipts, offset in part by payments in the ordinary course of business.

During fiscal 2013, as a result of net income and a $4.0 million reduction in accounts receivable, the Company generated $7.2 million of cash in operating activities compared to cash utilized by operating activities of $6.6 million in fiscal 2012.

Cash flows from investing activities

Cash used for investing activities primarily relates to funds used for capital expenditures in property, plant, and equipment and software development. The Company's investing activities used $1.3 million during fiscal 2013 and consisted primarily of costs for the acquisition of computer systems and equipment, and software enhancements for our ATFS technology. This is a decrease of $0.8 million from cash used in investing activities in fiscal 2012.

Cash flows from financing activities

The Company's financing activities utilized $6.4 million of cash during fiscal 2013 as compared to providing $10.9 million in fiscal 2012. The principal uses of cash were $10.0 million for the repurchase of Preferred Stock, $8.5 million for the repayments of the Company's Line of Credit and $1.5 million payment of Preferred Stock dividends. These were offset, in part, by $15.0 million of proceeds from the Term Loan.

Outlook

We expect to use our cash, cash equivalents, and credit facilities for working capital and general corporate purposes, products, technologies, property, plant, and equipment, the payment of contractual and other legal obligations, including scheduled interest payments on credit facilities and dividends on Preferred Stock, the potential acquisition of businesses, and/or the purchase, redemption, or retirement of our credit facilities and Preferred Stock. We expect that net sales of our currently marketed products, combined with availability under our lines of credit, should continue to provide us sufficient funds for fiscal 2014. At this time, however, we cannot accurately predict the effect of certain developments on our anticipated results in fiscal 2015 and beyond because of factors such as the degree of market acceptance, the impact of competition, the effectiveness of our sales and marketing efforts, and the outcome of our efforts to develop new products.

Through the current term of the Line of Credit with PNC Bank we expect to maintain, per our bank covenant requirement, a minimum Tangible Net Worth of $15.0 million, a maximum operating leverage ratio of 3.0, which will reduce to 2.9 as of February 28, 2014 and will remain as that level at all times thereafter, and a minimum fixed charge ration of 1.1.

Off-Balance Sheet Arrangements

There were no off-balance sheet arrangements during either fiscal 2013 or fiscal 2012 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 shareholders.

Board of Directors Actions

On February 15, 2013, the Board of Directors decided to voluntarily deregister the Company's Common Stock under Section 12(g) of the Securities Exchange Act of 1934. As a result of the deregistration, the Company's reporting obligations to the Securities and Exchange Commission ("SEC"), including its obligations to file annual, quarterly, and current reports on Forms 10-K, 10-Q, and 8-K, is suspended. Other SEC filing requirements will terminate upon the effective date of the Form 15, which is expected to occur on June 25, 2013.

The Company's decision to deregister was made primarily in light of our size and market capitalization, and the high costs and demands on senior management's time of our ongoing compliance with SEC and Sarbanes-Oxley reporting requirements. We expect to recognize substantial cost savings associated with this decision, in addition to allowing senior management to devote more resources to the core business of ETC.

Despite the deregistration, ETC intends to continue to prepare and publish quarterly and annual financial results. The Company also expects that the Company's Common Stock will continue to be traded in the over-the-counter market under the ticker symbol "ETCC".

MANAGEMENT'S REPORT

Management is responsible for the preparation as well as the integrity and objectivity of the Environmental Tectonics Corporation financial statements. These financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and necessarily include amounts that represent the best estimates and judgments of management.

Environmental Tectonics Corporation maintains an accounting system of internal controls to provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition and that financial records are reliable for preparing financial statements and maintaining accountability for assets. Reasonable assurance recognizes that the cost of a system of internal controls should not exceed its benefits and that the evaluation of these factors requires estimates and judgments by management. The internal control system includes the selection and training of management and supervisory personnel; an organizational structure providing for delegation of authority and establishment of responsibilities; communication of requirements for compliance with approved accounting control and business practices throughout the organization; and business planning and review.

McGladrey LLP, our independent auditor, is engaged to audit and report on these financial statements. Their audit is conducted in accordance with auditing standards generally accepted in the United States of America. Those standards require that they plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

The Audit Committee of the Board of Directors meets regularly with management, and our independent auditor to review matters relating to financial reporting, internal controls, and auditing. Management and our independent auditor each have direct and confidential access to this committee.

William F. Mitchell President and Chief Executive Officer	Robert L. Laurent, Jr. Chief Financial Officer

McGladrey LLP

McGladrey

Independent Auditor's Report

To the Board of Directors
Environmental Tectonics Corporation
Southampton, Pennsylvania

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Environmental Tectonics Corporation and its subsidiaries (the "Company") which comprise the consolidated balance sheets as of February 22, 2013 and February 24, 2012, and the related consolidated statements of income and comprehensive income, changes in shareholder's equity and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audit as of and for the year ended February 22, 2013, in accordance with auditing standards generally accepted in the United States of America. We conducted our audit as of and for the year ended February 24, 2012, in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. These procedures include examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Environmental Tectonics Corporation and its subsidiaries as of February 22, 2013 and February 24, 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

McGladrey LLP

Blue Bell, Pennsylvania
May 23, 2013

CONSOLIDATED BALANCE SHEETS

(in thousands, except share information)	February 22, 2013	February 24, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$ 2,877	$ 3,425
Restricted cash	6,162	6,000
Accounts receivable, net	6,666	10,695
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	19,949	18,766
Inventories, net	3,727	4,145
Deferred tax assets, current	2,193	4,170
Prepaid expenses and other current assets	1,297	830
Total current assets	42,871	48,031
Property, plant and equipment, at cost, net	14,609	14,860
Capitalized software development costs, net	378	666
Deferred tax assets, non-current, net	2,619	4,190
Other assets	91	39
Total assets	**$ 60,568**	**$ 67,786**
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt obligations	$ 3,600	$ 8
Accounts payable, trade	4,431	5,639
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	2,662	6,519
Customer deposits	2,818	3,425
Accrued income taxes	280	148
Accrued interest and dividends	483	941
Other accrued liabilities, current	3,462	3,565
Total current liabilities	17,736	20,245
Long-term obligations, less current portion:		
Credit facility payable to bank	7,585	16,716
Term loan	11,000	-
Total long-term debt obligations, less current portion	18,585	16,716
Other accrued liabilities, non-current	28	-
Total liabilities	36,349	36,961
Commitments and contingencies		
Shareholders' equity:		
Cumulative convertible participating Preferred Stock, Series D, $0.05 par value, 11,000 shares authorized; 0 and 386 shares outstanding as of February 22, 2013 and February 24, 2012, respectively	-	386
Cumulative convertible participating Preferred Stock, Series E, $0.05 par value, 25,000 shares authorized; 12,127 and 21,741 shares outstanding as of February 22, 2013 and February 24, 2012, respectively	12,127	21,741
Common Stock, $0.05 par value, 50,000,000 shares authorized; 9,180,161 and 9,134,403 shares issued and outstanding as of February 22, 2013 and February 24, 2012, respectively	459	456
Additional paid-in capital	9,924	9,892
Retained earnings (accumulated deficit)	2,251	(1,186)
Accumulated other comprehensive loss	(597)	(505)
Total shareholders' equity before non-controlling interest	24,164	30,784
Non-controlling interest	55	41
Total shareholders' equity	24,219	30,825
Total liabilities and shareholders' equity	**$ 60,568**	**$ 67,786**

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

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

	Fiscal year ended	
(in thousands, except per share information)	**February 22, 2013**	**February 24, 2012**
Net sales	$ 62,773	$ 66,294
Cost of goods sold	37,904	42,763
Gross profit	24,869	23,531
Operating expenses:		
Selling and marketing	5,570	5,481
General and administrative	8,186	8,513
Research and development	1,169	1,400
Operating expenses total	14,925	15,394
Operating income	9,944	8,137
Other expenses:		
Interest expense, net	1,005	734
Other expense (income), net	118	(85)
Other expenses total	1,123	649
Income before income taxes	8,821	7,488
Provision for income taxes	3,859	2,620
Net income	4,962	4,868
(Income) expense attributable to non-controlling interest	(14)	5
Net income attributable to Environmental Tectonics Corporation	**4,948**	**4,873**
Foreign currency translation adjustment and unrealized loss on cash flow hedge	(92)	(133)
Comprehensive income	$ 4,856	$ 4,740
Preferred Stock dividends	(1,511)	(2,208)
Income attributable to common and participating shareholders	$ 3,437	$ 2,665
Per share information:		
Basic earnings per common and participating share:		
Distributed earnings per share:		
Common	$ -	$ -
Preferred	$ 0.17	$ 0.20
Undistributed earnings per share:		
Common	$ 0.19	$ 0.13
Preferred	$ 0.19	$ 0.13
Diluted earnings per share	**$ 0.19**	**$ 0.13**
Basic weighted average common and participating shares:		
Common weighted average number of shares	9,149	9,114
Participating preferred shares	9,063	11,095
Total basic weighted average common and participating shares	18,212	20,209
Diluted weighted average shares:		
Basic weighted average common and participating shares	18,212	20,209
Dilutive effect of stock warrants and options	163	288
Total diluted weighted average shares	18,375	20,497

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

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(in thousands, except share information)	Preferred Stock	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Loss	(Accumulated Deficit) / Retained Earnings	Total Shareholders' Equity
Balance, February 25, 2011	$ 22,127	9,104,601	$ 455	$ 11,932	$ (372)	$ (6,059)	$ 28,129
Less: Prior year non-controlling interest	-	-	-	-	-	-	(46)
Net income attributable to Environmental Tectonics Corporation	-	-	-	-	-	4,873	4,873
Foreign currency translation adjustment	-	-	-	-	(133)	-	(133)
Preferred Stock dividends	-	-	-	(2,208)	-	-	(2,208)
Stock compensation expense	-	-	-	101	-	-	101
Issuance of stock under employee stock purchase plan and Board of Director's compensation	-	29,802	1	67	-	-	68
Balance before non-controlling interest, February 24, 2012	22,127	9,134,403	456	9,892	(505)	(1,186)	30,784
Non-controlling interest	-	-	-	-	-	-	41
Balance, February 24, 2012	**22,127**	**9,134,403**	**456**	**9,892**	**(505)**	**(1,186)**	**30,825**
Less: Prior year non-controlling interest	-	-	-	-	-	-	(41)
Net income attributable to Environmental Tectonics Corporation	-	-	-	-	-	4,948	4,948
Foreign currency translation adjustment	-	-	-	-	(64)	-	(64)
Unrealized loss on cash flow hedge	-	-	-	-	(28)	-	(28)
Preferred Stock dividends	-	-	-	-	-	(1,511)	(1,511)
Stock compensation expense	-	-	-	69	-	-	69
Issuance of stock under employee stock purchase plan and Board of Director's compensation	-	45,758	3	66	-	-	69
Repurchase of Series D Preferred Stock	(386)	-	-	-	-	-	(386)
Repurchase of Series E Preferred Stock	(9,614)	-	-	-	-	-	(9,614)
Preferred Stock repurchase costs	-	-	-	(103)	-	-	(103)
Balance before non-controlling interest, February 22, 2013	12,127	9,180,161	459	9,924	(597)	2,251	24,164
Non-controlling interest	-	-	-	-	-	-	55
Balance, February 22, 2013	**$ 12,127**	**9,180,161**	**$ 459**	**$ 9,924**	**$ (597)**	**$ 2,251**	**$ 24,219**

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)	Fiscal year ended February 22, 2013	February 24, 2012
Cash flows from operating activities:		
Net income	$ 4,962	$ 4,868
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,843	1,760
Deferred tax assets	3,458	1,638
Increase (decrease) in valuation allowance for deferred tax assets	90	(272)
Decrease in allowances for accounts receivable and inventories, net	(18)	(126)
Accretion of loan origination deferred charge and deferred financing costs	145	156
Stock compensation expense	69	101
Changes in operating assets and liabilities:		
Accounts receivable	4,029	(5,969)
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	(1,183)	(8,395)
Inventories	436	(983)
Prepaid expenses and other assets	(533)	(265)
Accounts payable, trade	(1,208)	1,332
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	(3,857)	(1,015)
Customer deposits	(607)	(482)
Accrued income taxes	132	120
Accrued interest and dividends	(458)	216
Other accrued liabilities	(103)	707
Net cash provided by (used in) operating activities	**7,197**	**(6,609)**
Cash flows from investing activities:		
Acquisition of property, plant, and equipment	(1,278)	(1,914)
Capitalized software development costs	(26)	(230)
Net cash used in investing activities	**(1,304)**	**(2,144)**
Cash flows from financing activities:		
Proceeds from Term Loan	15,000	-
(Repayments) borrowings under line of credit	(8,531)	13,675
Payments of Preferred Stock dividends	(1,511)	(2,208)
Increase in restricted cash	(162)	(393)
Payments on the Term Loan and of other debt obligations	(1,008)	(254)
Payments of deferred financing and Preferred Stock repurchase costs	(234)	-
Issuance of Common Stock	69	68
Repurchase of Preferred Stock, Series D	(386)	-
Repurchase of Preferred Stock, Series E	(9,614)	-
Net cash (used in) provided by financing activities	**(6,377)**	**10,888**
Effect of exchange rate changes on cash	(64)	(133)
Net (decrease) increase in cash	(548)	2,002
Cash at beginning of period	3,425	1,423
Cash at end of period	**$ 2,877**	**$ 3,425**
Supplemental schedule of cash flow information:		
Interest paid	$ 1,102	$ 427
Income taxes paid	$ 225	$ 737
Supplemental information on non-cash operating and investing activities:		
Accrued Preferred Stock dividends	$ 407	$ 552
Unrealized loss on cash flow hedge	$ 28	$ -

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share information)

Description of Business

ETC was incorporated in 1969 in Pennsylvania. For over four decades, we have provided our customers with products, service, and support. Innovation, continuous technological improvement and enhancement, and product quality are core values that are critical to our success. We are a significant supplier and innovator in the following product areas: (i) software driven products and services used to create and monitor the physiological effects of flight, including high performance jet tactical flight simulation, upset recovery and spatial disorientation, and both suborbital and orbital commercial human spaceflight; collectively, Aircrew Training Systems ("ATS"); (ii) altitude (hypobaric) chambers; (iii) the Advanced Disaster Management Simulator ("ADMS"); (iv) steam and gas (ethylene oxide) sterilizers; (v) environmental testing and simulation devices; and (vi) hyperbaric (100% oxygen) chambers for one person (monoplace chambers).

We operate in two primary business segments, Aerospace Solutions ("Aerospace") and Commercial/ Industrial Systems ("CIS"). Aerospace encompasses the design, manufacture, and sale of: (i) Aircrew Training Systems; (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); and (iv) ADMS, as well as integrated logistics support for customers who purchase these products or similar products manufactured by other parties. These products and services provide customers with an offering of comprehensive solutions for improved readiness and reduced operational costs. Sales of our Aerospace products are made principally to U.S. and foreign government agencies. CIS encompasses the design, manufacture, and sale of: (i) steam and gas (ethylene oxide) sterilizers; (ii) environmental testing and simulation devices; and (iii) hyperbaric (100% oxygen) chambers for one person (monoplace chambers), as well as parts and service support for customers who purchase these products or similar products manufactured by other parties. Sales of our CIS products are made principally to the healthcare, pharmaceutical, and automotive industries. Net sales, operating income, identifiable assets, and other financial information regarding our segments may be found in Note 9 – Business Segment Information.

The Company's fiscal year is the 52- or 53-week annual accounting period ending the last Friday in February. Both fiscal 2013 and fiscal 2012 are 52-week periods. Certain amounts from prior consolidated financial statements have been reclassified to conform to the presentation in fiscal 2013.

Sales Backlog

Below is a breakdown of the Company's February 22, 2013 sales backlog (amounts in thousands, except percentages):

	Business segment			
Geographic area	**Aerospace**	**CIS**	**Total**	**%**
Domestic	$ 604	$ 5,529	$ 6,133	12.7%
U.S. Government	17,817	-	17,817	36.7
International	23,271	1,273	24,544	50.6
Total	**$ 41,692**	**$ 6,802**	**$ 48,494**	**100.0%**
% of Total	86.0%	14.0%	100.0%	

Our sales backlog as of February 22, 2013, for work to be performed and revenue to be recognized under written agreements after such dates, was $48,494. Of the February 22, 2013 sales backlog, three product lines (ATS, Chambers, and Sterilizers) represented at least 10% of the total backlog (ATS was $12,879, or 26.6%, of the total sales backlog; Chambers was $18,807, or 38.8%, of the total sales backlog; Sterilizers was $4,864, or 10.0%, of the total sales backlog). ETC-PZL totaled $5,533, or 11.4% of the total sales backlog as of February 22, 2013. Of the February 22, 2013 sales backlog, $9,260 represents two international contracts for multiple Aerospace products. Approximately 95.7% of the U.S. Government sales backlog relates to three contracts.

1. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of ETC, ETC-PZL Aerospace Industries Sp. z o.o. ("ETC-PZL"), our 95%-owned subsidiary in Warsaw, Poland, and our 99%-owned subsidiary Environmental Tectonics Corporation (Europe) Limited ("ETC-Europe"). "ETC-SH" refers to the Company's corporate headquarters and main production plant located in Southampton, Pennsylvania, USA. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, 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 ("POC") method, claims receivable, inventories, and income taxes.

Fair Value of Financial Instruments

The carrying amounts of cash, accounts receivable, accounts payable, and bank debt approximate fair value because of the short maturity associated with each of these instruments. Other assets and liabilities that are measured at fair value on a recurring basis include the unrealized gains or losses on interest rate swap contracts. For these assets and liabilities, we use significant other observable market data or assumptions (Level 2 inputs as defined in the accounting guidance) that we believe market participants would use in pricing similar assets or liabilities, including assumptions about counterparty risk. Our fair value estimates reflect an income approach based on the terms of the interest rate contracts and inputs corroborated by observable market data including interest rate curves.

Revenue Recognition

Revenue, which is recorded net of any applicable sales tax, is recognized using three methods:

On long-term contracts, with a contract value over $250 and a minimum completion period of six months, the POC method is applied based on costs incurred from inception to date as a percentage of estimated total costs required to fulfill the contract. This percentage is then multiplied by the total estimated contract value to determine the cumulative amount of revenue to be recognized, from which previously recognized revenue would be subtracted to determine 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 an 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 (i.e. milestone payments) in excess of revenue recognized on uncompleted long-term contracts are reflected as a 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 that 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. Costs related to post shipment obligations, including field installation, warranty, and any additional contracted items are included in the estimated total costs required to fulfill the contract. 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 POC method involves significant estimates, both at inception and throughout the performance period. Some of our long-term contracts contain provisions that require us to pay liquidated damages if we are responsible for the failure to meet specified contractual milestone dates and the applicable customer asserts a claim under these provisions. Management uses its best judgment to estimate not only the cost to perform the work, but also the price that will eventually be paid by our customers on such contracts.

For contracts under $250, or contracts to be completed in less than six months, and where there are no post-shipment services included in the contract (such as installation and customer acceptance), the completed contract method is applied and revenue is recognized on the date that the finished product is shipped to the customer. Estimated warranty costs for these contracts are accrued and this accrual is adjusted periodically based on actual warranty expenses and the amount and type of products shipped. Revenue derived from 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. There are no post contract expenses associated with these types of contracts.

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.

Cash and Cash Equivalents

Cash includes 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 $250. During each fiscal year, the Company periodically has cash and cash equivalents in excess of insured amounts.

Restricted Cash

Restricted cash was $6,162 as of February 22, 2013 compared to $6,000 as of February 24, 2012. Restricted cash is comprised primarily of collateral for a dedicated line of credit in the amount of $5,422 with PNC Bank (the "Dedicated Line of Credit"), which the Company uses to satisfy performance bond and repayment guarantee requirements for an international contract. Use of this Dedicated Line of Credit is restricted to funding contract performance and repayment guarantee requirements under this specific contract. As security for this Dedicated Line of Credit, the Company has deposited $5,422 in a certificate of deposit with PNC Bank, National Association ("PNC Bank"). ETC is obligated to pay a fee, due quarterly, of three percent (3%) per year for the Dedicated Line of Credit.

Accounts Receivable and Concentration of Credit Risk

The Company performs ongoing credit evaluations of its customers and adjusts credit limits based on payment history and the customer's current creditworthiness. Terms are cash upon delivery, except where satisfactory open account credit is established, in which case terms are generally payment net thirty (30) days from the date of the invoice. Accounts receivable are deemed past due if payment is not received by the payment due date. Overdue payments are subject to interest penalty of the delinquent amount at the rate of one and one-half percent (1.5%) per month. The Company continuously monitors collections and payments from its customers, and maintains a provision for estimated credit losses based on historical experience and any specific customer collection issues that are identified. While credit losses have historically been within the Company's expectations and the provisions established, we cannot guarantee that the Company will continue to experience the same credit loss rates. Additionally, as a result of the concentration of international receivables, the Company cannot predict the effect, if any, that geopolitical disputes and financial constraints will have on the ultimate collection of its international receivables. Amounts due under contracts related to agencies of a foreign government totaled $356 or 5.5%, of total net accounts receivable as of February 22, 2013. Subsequent to fiscal year end, as of the date of issuance of the consolidated financial statements, approximately 82.0% of these receivables have been collected. See Note 3 – Accounts Receivable for additional disclosures related to our accounts receivable.

Inventories

Inventories are valued at the lower of cost or market. Cost is determined principally by the first-in, first-out method ("FIFO method"). The costs of finished goods and work-in-process inventories include material, direct engineering, manufacturing labor, and overhead components. Overheads allocated to inventory cost are only those directly related to our manufacturing activities. Where necessary, provision is made for obsolete, slow-moving, or damaged inventory. This provision represents the difference between the cost of the inventory and its estimated market value.

In accordance with accounting principles generally accepted in the United States of America, the Company may capitalize certain costs of simulation equipment into property, plant, and equipment. This equipment may be used to provide training or as a demonstration device to market the technology, and may be sold as a product if appropriate. During fiscal 2012, $980 of engineering costs associated with our ATFS-400-25 PHOENIX High Performance Human Centrifuge demonstration unit was transferred from inventory into property, plant, and equipment and is currently being depreciated. No such transfers occurred during fiscal 2013.

Property, Plant, and Equipment

Property, plant, and equipment are stated at cost, and are depreciated over their estimated useful lives using the straight-line method for financial reporting purposes. Buildings and building additions are depreciated over 40 years; machinery and equipment, 3 to 20 years; office furniture and equipment, 10 years; and building improvements, 5 to 10 years. The Company manufactures certain equipment that is used primarily for both research and demonstration purposes to support its sales effort and is not listed for sale, although sales of such demonstration equipment are not precluded. The gross value of demonstration equipment was $13,419 and $12,605 as of February 22, 2013 and February 24, 2012, respectively. The net book value of demonstration equipment was $9,398 and $9,397 as of February 22, 2013 and February 24, 2012, respectively. Upon sale of such demonstration devices, their costs, net of accumulated depreciation, are transferred to cost of sales. Upon sale or retirement of property, plant, and equipment, the costs and related accumulated depreciation are eliminated from the accounts with any resulting gains or losses. In fiscal 2013, $347 of machinery and equipment primarily associated with ETC-PZL, all of which was fully depreciated, was retired.

Capitalized Software Development Costs

The Company capitalizes the qualifying costs of developing software contained in certain products. Capitalization of such costs commences when technological feasibility has been established in accordance with the Financial Accounting Standards Board's ("FASB") guidance on accounting for the costs of computer software to be sold, leased, or otherwise marketed. Technological feasibility is defined as the point in time when the Company has completed all planning, designing, coding, and testing activities that are necessary to establish that a software product can be produced to meet its design specifications, including functions, features, and technical performance requirements. When the software is ready for commercial release, capitalization of development costs cease and amortization commences on a straight-line basis over a period ranging from three (3) to five (5) years, depending upon the life of the product. The establishment of technological feasibility and the ongoing assessment of the recoverability of these costs require considerable judgment by management with respect to certain external factors including, but not limited to, anticipated future gross product revenue, estimated economic product lives, and changes in software and hardware technology. Software amortization totaled $314 and $367 in fiscal 2013 and fiscal 2012, respectively. Estimated software amortization, which is based on existing capitalized software, for each of the next five (5) fiscal years is as follows: $197 in fiscal 2014; $117 in fiscal 2015; $50 in fiscal 2016; $12 in fiscal 2017, and $2 in fiscal 2018 and beyond.

Research and Development Costs

Research and development costs, which relate primarily to the development, design, and testing of products, are expensed as incurred. The Company enters into research grants with various government entities, both in the United States and internationally. During fiscal 2013 and fiscal 2012, the Company was involved with five (5) and seven (7) such grants, respectively. Payments received under these grants are recorded as a reduction of research and development costs. Such payments totaled $1,167 in fiscal 2013 and $1,976 in fiscal 2012. Research and development expenses, which totaled $2,336 in fiscal 2013 and $3,376 in fiscal 2012, include spending for potential new products and technologies and work performed under government grant programs, both in the United States and internationally. This spending, net of grant payments from the United States, and the governments of Poland and Turkey, as detailed above, was $1,169 for fiscal 2013 compared to $1,400 for fiscal 2012.

Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes, as well as the valuation of net loss carryforwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the potential realization of the related deferred tax asset.

Significant judgments and estimates are required in determining the provision for taxes, including judgments and estimates regarding the realization of deferred tax assets and the ultimate outcomes of tax-related contingencies. During the normal course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. A liability is recognized, including interest, or a tax asset is reduced, for the anticipated outcome of tax audits. These amounts are adjusted in light of changing facts and circumstances.

Long-Lived Assets

The Company reviews its property, plant, 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 undiscounted future cash flows. The results of impairment tests are subject to management's estimates and assumptions of projected cash flows and operating results; actual results may differ. There were no impairment losses recorded in either fiscal 2013 or fiscal 2012.

Share-Based Compensation

Share-based compensation expense is measured at the stock option grant date, based on the fair value of the award, and is recorded primarily to general and administrative expense. The Company uses the Black-Scholes option-pricing model and the straight-line attribution approach to determine the fair value of share-based awards in accordance with Accounting Standards Codification ("ASC") 718, Compensation. This option-pricing model requires the input of highly subjective assumptions, including the option's expected term, the price volatility of the underlying stock, risk-free rates of return, dividend yield, and expected forfeitures. The expected term of an award is no less than the award vesting period and is based on the Company's historical experience. The expected stock price volatility is based on the Company's historical stock prices. The risk-free interest rate is approximated using rates available on U.S. Treasury securities in effect at the time of grant with a remaining term similar to the award's expected life. The Company uses a dividend yield of zero in the Black-Scholes option valuation model as it does not anticipate paying cash dividends in the near future. The Company is required to estimate forfeitures at the time of grant, and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and record share-based compensation expense for only those awards that are expected to vest as the requisite service is rendered. The guidance requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from these estimates. The Company typically issues new shares of Common Stock upon the exercise of stock options, as opposed to using treasury shares. There were no options granted in fiscal 2013; there were 10,000 options granted in fiscal 2012.

Advertising Costs

The Company expenses advertising costs, which include trade shows, as incurred. Advertising costs were $444 and $539 in fiscal 2013 and fiscal 2012, respectively.

Warranty Costs

The Company provides warranties against defects in materials and workmanship in our products. Warranty periods for our products generally range from ninety (90) days to two (2) years. The Company maintains a general provision for estimated expenses of providing service under these warranties. Non-warranty service is billed to the customer as performed. The assumptions we use to estimate warranty accruals are evaluated periodically in light of actual experience and management's estimates of future claims, and, when appropriate, the accruals are adjusted. Our determination of the appropriate level of warranty accrual is subjective and based on estimates, and actual experience may be different than our accruals.

Earnings per Share

The Company utilizes the two-class method for computing and presenting earnings per share. The Company currently has one class of Common Stock (the "Common Stock") and two classes of cumulative participating Preferred Stock, Series D and Series E (the "Preferred Stock"). Under its terms, the Preferred Stock is entitled to participate in any cash dividends on a one-for-one basis for the equivalent converted common shares if the Preferred Stock were to be converted by the holder by the dividend record date; therefore, the Preferred Stock is considered a participating security requiring the two-class method for the computation and presentation of net income per share – basic.

The two-class computation method for each period segregates basic earnings per common and participating share into two categories: distributed earnings per share (i.e., the Preferred Stock stated dividend) and undistributed earnings per share, which allocates earnings after subtracting the Preferred Stock dividend to the total of weighted average common and participating shares outstanding plus equivalent converted common shares related to the Preferred Stock. Basic earnings per common and participating share excludes the effect of Common Stock equivalents, and is computed using the two-class computation method.

Diluted earnings per share reflects the potential dilution that could result if securities or other contracts to issue Common Stock were exercised or converted into Common Stock. Diluted earnings per share continues to be computed using the if-converted method. Diluted earnings per share assumes the exercise of stock options and warrants using the treasury stock method. If the effect of the conversion of any financial instruments would be anti-dilutive, it is excluded from the diluted earnings per share calculation.

As of February 22, 2013, there was $12,127 of cumulative convertible participating Series E Preferred Stock convertible at an exercise price of $2.00 per share, equating to 6,063,321 shares of Common Stock, issued in July 2009.

As of February 24, 2012, there was $22,127 of cumulative convertible participating Preferred Stock. These instruments were convertible at exercise prices of:

- Series D Preferred Stock of $55 at $0.94 per share, equating to 58,511 shares of Common Stock, issued in April 2009;
- Series D Preferred Stock of $100 at $1.11 per share, equating to 90,090 shares of Common Stock, issued in July 2009;
- Series D Preferred Stock of $231 at $3.02 per share, equating to 76,490 shares of Common Stock, issued in October 2010; and
- Series E Preferred Stock of $21,741 at $2.00 per share, equating to 10,870,321 shares of Common Stock, issued in July 2009.

On February 20, 2009, in connection with the issuance of a $2,000 promissory note, the Company issued 200,000 warrants to purchase 143,885 shares of the Company's Common Stock at $1.39 per share. Additionally, on July 2, 2009, in consideration of an increase of the guarantee on the 2007 PNC Credit Facility (as defined in Note 6 – Long-Term Obligations and Credit Arrangements), the Company issued 500,000 warrants to purchase 450,450 shares of the Company's Common Stock at $1.11 per share. On January 4, 2011, the Company entered into amendments to these warrants to remove a provision in each of the warrants which provided anti-dilution protection in the event the Company issued securities at a price below the exercise price set forth in the warrants.

As of February 22, 2013 and February 24, 2012, there were outstanding options to purchase the Company's Common Stock totaling 219,917 and 270,921 shares at an average price of $4.23 and $4.35 per share, respectively. Due to the conversion price of certain Common Stock options, 219,917 and 260,921 shares were excluded from the calculation of diluted earnings per share as of February 22, 2013 and February 24, 2012, respectively, because the effect of their conversion would be anti-dilutive.

Recent Accounting Pronouncements

In June 2011, the FASB issued Accounting Standards Update ("ASU") No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. ASU 2011-05 amends the FASB Accounting Standards Codification ("Codification") to allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments to the Codification in ASU 2011-05 do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income.

In December 2011, the FASB issued ASU No. 2011-12, Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. Among the new provisions in ASU 2011-05 was a requirement for entities to present reclassification adjustments out of accumulated other comprehensive income by component in both the statement in which net income is presented and the statement in which other comprehensive income is presented (for both interim and annual financial statements); accordingly, this requirement is indefinitely deferred by ASU 2011-12 and will be further deliberated by the FASB at a future date.

The Company adopted this guidance during the thirteen week period ended February 24, 2012, and chose to present other comprehensive income within the accompanying Consolidated Statements of Income and Comprehensive Income. The effect of this amended guidance has been retrospectively applied to all periods presented.

In July 2012, the FASB issued ASU No. 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment, which amends the guidance in ASC 350-30 on testing indefinite-lived intangible assets, other than goodwill, for impairment. Under ASU 2012-02, an entity testing an indefinite-lived intangible asset for impairment has the option of performing a qualitative assessment before calculating the fair value of the asset. If the entity determines, on the basis of qualitative factors, that the fair value of the indefinite-lived intangible asset is not more likely than not (i.e., a likelihood of more than fifty percent) impaired, the entity would not need to calculate the fair value of the asset. ASU 2012-02 does not revise the requirement to test indefinite-lived intangible assets annually for impairment. In addition, ASU 2012-02 does not amend the requirement to test these assets for impairment between annual tests if there is a change in events or circumstances; however, it does revise the examples of events and circumstances that an entity should consider in interim periods. ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012; early adoption is permitted. The effect of this amended guidance is not expected to have a significant impact on the consolidated financial statements.

2. Accounts Receivable

The components of accounts receivable are as follows:

	February 22, 2013	February 24, 2012
U.S. Government	$ 3,075	$ 4,305
U.S. Commercial	1,904	2,994
International	2,088	3,797
	7,066	11,095
Less: allowance for doubtful accounts	(400)	(400)
Accounts receivable, net	**$ 6,666**	**$ 10,695**

3. Costs and Estimated Earnings on Uncompleted Contracts

The following is a summary of long-term contracts in progress:

	February 22, 2013	February 24,2012
Cost incurred on uncompleted long-term contracts	$ 103,790	$ 80,543
Estimated earnings	62,258	48,748
	166,048	129,291
Less: billings to date	(148,761)	(117,044)
	$ 17,287	**$ 12,247**

Included in accompanying balance sheets under the following captions:

	February 22, 2013	February 24, 2012
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	$ 19,949	$ 18,766
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	(2,662)	(6,519)
	$ 17,287	**$ 12,247**

Included in billings in excess of costs and estimated earnings on uncompleted long-term contracts is a provision for unexpected losses on contracts of $200 in fiscal 2013 and fiscal 2012.

In accordance with industry practices, costs and estimated earnings in excess of billings on uncompleted long-term contracts are classified as current even though a portion of these amounts may not be realized within one year.

4. Inventories

Inventories are valued at the lower of cost or market using the FIFO method and consist of the following:

	February 22, 2013	February 24, 2012
Raw materials	$ 152	$ 42
Work in progress	3,575	4,103
Inventories, net	**$ 3,727**	**$ 4,145**

Inventory is presented net of an allowance for obsolescence of $1,139 (raw material $41 and work in process $1,098), and $1,157 (raw material $50 and work in process $1,107) as of February 22, 2013 and February 24, 2012, respectively.

In accordance with accounting principles generally accepted in the United States of America, the Company may capitalize certain costs of simulation equipment into property, plant, and equipment. This equipment may be used to provide training or as a demonstration device to market the technology, and may be sold as a product if appropriate. During fiscal 2012, $980 of engineering costs associated with our ATFS-400-25 PHOENIX High Performance Human Centrifuge demonstration unit, was transferred from inventory into property, plant, and equipment and is currently being depreciated. No such transfers occurred during fiscal 2013.

5. Property, Plant, and Equipment

The following is a summary of property, plant, and equipment, at cost by classification, and net collecively:

	February 22, 2013	February 24, 2012
Land	$ 100	$ 100
Buildings and building additions	3,851	3,851
Machinery and equipment	11,410	11,484
Demonstration equipment	13,419	12,605
Office furniture and equipment	1,316	1,301
Building improvements	3,057	3,003
Construction in process	121	-
	33,275	32,344
Less: accumulated depreciation	(18,666)	(17,484)
Property, plant, and equipment, net	**$ 14,609**	**$ 14,860**

Depreciation expense for fiscal 2013 and fiscal 2012 was $1,529 and $1,393, respectively.

As of both February 22, 2013 and February 24, 2012, substantially all of the Company's long-lived assets were located in the United States of America.

6. Long-Term Obligations and Related Equity Arrangements

2009 Lenfest Financing Transaction

On April 24, 2009, the Company entered into a transaction (the "2009 Lenfest Financing Transaction") with Mr. Lenfest, that provided for, among other things, the following:

(i) a $7,500 credit facility provided by Mr. Lenfest to ETC (the "Lenfest Credit Facility"), which has expired;

(ii) the exchange of the senior subordinated convertible promissory note in the original principal amount of $10,000 issued by ETC to Mr. Lenfest on February 18, 2003, together with all accrued interest and warrants issuable under the note, and all Series B Preferred Stock and Series C Preferred Stock held by Mr. Lenfest, together with all accrued dividends thereon, for a new class of preferred stock, Series E Preferred Stock, the terms of which are described below; and

(iii) the guarantee by Mr. Lenfest of all of ETC's obligations to PNC Bank in connection with an increase of the existing $15,000 revolving line of credit with PNC Bank (the "2007 PNC Credit Facility") to $20,000, and in connection with this guarantee, the pledge by Mr. Lenfest to PNC Bank of $10,000 in marketable securities to secure ETC's obligations to PNC Bank (the "Lenfest Pledge").

2012 Financial Restructuring

On September 28, 2012, the Company entered into transactions, collectively the 2012 Financial Restructuring, that provided for, among other things, the following:

(i) the Company's Line of Credit with PNC Bank was reduced from $20,000 to $15,000; however, the term of the Line of Credit was extended twenty-eight (28) months, from June 30, 2013 to October 31, 2015.

(ii) PNC Bank provided to the Company a new five (5) year $15,000 Term Loan. The Company used $10,000 of the proceeds from the Term Loan to repurchase and retire 10,000 shares of its Series D and Series E Preferred Stock owned by Mr. Lenfest at the stated price of $1,000 per share. The remaining $5,000 was used to repay indebtedness currently outstanding to PNC Bank and to pay Mr. Lenfest $417 of interest due under the Lenfest Pledge, in cash, in lieu of Series D Preferred Stock. The $10,000 in marketable securities associated with the Lenfest Pledge has been returned to Mr. Lenfest and the Lenfest Pledge has been terminated; therefore, as of February 22, 2013, no interest has been accrued for under the Lenfest Pledge.

(iii) the Line of Credit is no longer guaranteed by Mr. Lenfest. Instead, the Line of Credit and Term Loan are secured by substantially all of the Company's assets. In addition, the Term Loan is guaranteed by Mr. Lenfest for a period of thirty (30) months, (i.e., until March 31, 2015), after which the guarantee will be removed.

(iv) following the close of the transactions on September 28, 2012, the dividend rate on the Series D and Series E Preferred Stock was reduced from ten percent (10%) to four percent (4%), subject to the future approval of the Company's Common Stock shareholders at the 2013 Annual Meeting of Shareholders.

The material agreements providing for these transactions are described below:

Loan Agreement

Effective September 28, 2012, ETC and PNC Bank entered into a Loan Agreement, which included ETC executing a Term Loan Note and the Line of Credit Note (as defined below). As set forth in the Loan Agreement, the Company's Line of Credit was reduced from $20,000 to $15,000; however, the term of the Line of Credit was extended twenty-eight (28) months, from June 30, 2013 to October 31, 2015. PNC Bank also provided to the Company a Term Loan of $15,000. The Company used $10,000 of the proceeds from the Term Loan to repurchase and retire 10,000 shares of the Series D and Series E Preferred Stock owned by Mr. Lenfest, at the stated price of $1,000 per share (as described in more detail below under the heading "Preferred Stock Repurchase Agreement"). The remaining $5,000 was used to repay indebtedness currently outstanding to PNC Bank and to pay Mr. Lenfest $417 of interest due under the Lenfest Pledge, in cash, in lieu of Series D Preferred Stock.

The Line of Credit is no longer guaranteed by Mr. Lenfest. Instead both the Line of Credit and the Term Loan are secured by substantially all of the Company's assets, including a mortgage on the Company's headquarters in Southampton, Pennsylvania.

The Term Loan is guaranteed by Mr. Lenfest for a period of thirty (30) months, (i.e., until March 31, 2015), after which the guarantee will be removed. The Company's obligation to repay the Term Loan is set forth in a Term Loan Note (the "Term Loan Note"). The interest rate on the Term Loan Note (currently 2.70%) will be based on the PNC Daily LIBOR Rate plus a margin of 2.25% to 2.75% depending on the Operating Leverage Ratio (currently 2.50%).

Borrowings under the Line of Credit will be available for working capital and other general business purposes and for issuances of letters of credit. Amounts borrowed under the Line of Credit may be borrowed, repaid, and re-borrowed from time to time until October 31, 2015. The Company's obligation to repay the advances under the Line of Credit is set forth in the Amended and Restated Committed Line of Credit Note (the "Line of Credit Note"). According to the Loan Agreement, at the Company's option, the interest rate on the Line of Credit Note will be based on either (i) the PNC Base Rate (currently 3.00%) plus a margin of -0.25% to 0.25% depending on the Company's Operating Leverage Ratio (currently 0.25%) or (ii) the PNC One-Month LIBOR Rate plus a margin of 2.25% to 2.75% (currently 2.70%) depending on the Operating Leverage Ratio (currently 2.50%).

On April 9, 2013, the Company entered into an amendment to the Loan Agreement that provides an enhanced investment and borrowing sweep feature that allows ETC to increase returns on idle cash balances and minimize interest expense on the Company's Line of Credit. With the sweep feature, excess cash in ETC's checking account is invested and automatically liquidated as needed to cover daily transactions. Effective as of the date of this amendment, the interest rate on the Line of Credit Note (currently 2.70%) will be based on the PNC Daily LIBOR Rate plus a margin of 2.25% to 2.75% depending on the Operating Leverage Ratio (currently 2.50%). See Note 15 – Subsequent Events for additional details.

The Company is also obligated to pay a fee of 0.25% for unused but available funds under the Line of Credit. As of February 22, 2013, the Company's availability under the Line of Credit was $6,557. This reflected cash borrowing under the Line of Credit of $7,585 and outstanding letters of credit of approximately $858.

As security for repayment of the Line of Credit Note and the Term Loan Note as noted above, the Company also concurrently entered into the Third Amended and Restated Reimbursement Agreement for Letters of Credit between ETC and PNC Bank dated September 28, 2012, a Security Agreement between ETC and PNC Bank dated September 28, 2012, a Pledge Agreement executed by ETC on September 28, 2012 in favor of PNC Bank ("Pledge Agreement"), an Amended and Restated Guaranty and Suretyship Agreement executed by Mr. Lenfest on September 28, 2012 in favor of PNC Bank, and an Open-End Mortgage and Security Agreement between ETC and PNC Bank dated September 28, 2012. Pursuant to the Pledge Agreement, the Company pledged to PNC as collateral the Company's ownership interest in certain subsidiaries of the Company.

The Loan Agreement contains affirmative and negative covenants that are customary for transactions of this type, including a minimum net worth, a maximum operating leverage ratio, and a minimum fixed charge coverage ratio, as well as limitations with respect to indebtedness, liens, investments, distributions, dispositions of assets, change of business, and transactions with affiliates. The financial covenants in the Loan Agreement, with which the Company is in compliance with as of February 22, 2013, are as follows:

- ETC must maintain a minimum Tangible Net Worth of $15,000.
- ETC must maintain an Operating Leverage Ratio (i.e., ratio of Senior Funded Debt to EBITDA, which is defined as earnings before interest, taxes, depreciation, and amortization) of less than 3.00 to 1 as of February 22, 2013. This ratio will reduce to 2.90 to 1 as of February 28, 2014, and will remain at that level at all times thereafter.
- ETC must maintain as of the end of each fiscal quarter, on a rolling four quarters basis, a Fixed Charge Coverage Ratio of at least 1.10 to 1.

The Loan Agreement provides for customary events of default, including the failure to pay any principal or interest when due, failure to comply with covenants, material misrepresentations, certain bankruptcy, insolvency or receivership events, imposition of certain judgments, and the liquidation of ETC. Upon an event of default under the Loan Agreement, including the non-payment of principal or interest, the obligations of the Company under the Loan Agreement may be accelerated and the assets securing the obligations secured.

Interest Rate Swap

On September 28, 2012, the Company entered into an interest rate swap agreement to protect against certain interest rate fluctuations of the LIBOR interest rate initially on $5,000 of the $15,000 variable rate Term Loan. The effective date of the interest rate swap was September 28, 2012, and it is scheduled to expire on September 28, 2017. The notional amount of $5,000 will decrease ratably over the duration of the interest rate swap agreement. The interest rate swap effectively fixes our LIBOR interest rate on the notional amount at a rate of 0.74% in excess of the margin. We have recognized the fair value of our interest rate swap as a long-term liability of approximately $28 as of February 22, 2013. We have designated our current interest rate swap as a cash flow hedge instrument. As of February 22, 2013, we have determined the hedge to be effective. See Note 14 – Fair Value Measurements and Interest Rate Swap for additional disclosures related to the interest rate swap.

Preferred Stock Repurchase Agreement

Effective September 28, 2012, ETC and Mr. Lenfest entered into a Preferred Stock Repurchase and Financial Restructuring Agreement.

Immediately following the closing of the Loan Agreement with PNC Bank, the Company purchased from Mr. Lenfest, at the stated price of $1,000 per share, (i) 386 shares of Series D Preferred Stock, representing all of the Company's issued and outstanding shares of Series D Preferred Stock, and (ii) 9,614 shares of Series E Preferred Stock, representing a significant portion of the Company's issued and outstanding Series E Preferred Stock. Mr. Lenfest is the only holder of the outstanding Series E Preferred Stock, and 12,127 shares of Series E Preferred Stock remain outstanding as of February 22, 2013.

Following the execution of the Preferred Stock Repurchase and Financial Restructuring Agreement, the dividend rate on the Series D and Series E Preferred Stock was reduced from ten percent (10%) to four percent (4%). The reduction of the Preferred Stock dividend will require the approval of the Company's shareholders at the 2013 Annual Meeting of Shareholders, and until that time Mr. Lenfest has agreed that all dividends on the outstanding Series E Preferred Stock will be paid at the rate of four percent (4%) per year.

Termination of Certain Lenfest Agreements

On September 28, 2012, upon the execution of the Preferred Stock Repurchase and Financial Restructuring Agreement described above, the following prior agreements between ETC and Mr. Lenfest were terminated: (i) Secured Credit Facility and Warrant Purchase Agreement between the Company and Mr. Lenfest, dated as of April 24, 2009; (ii) the Security Agreement, dated February 18, 2009, by the Company in favor of Mr. Lenfest; (iii) the Security Agreement, dated April 24, 2009, among the Company, Entertainment Technology Corporation, a defunct Pennsylvania corporation and once wholly-owned subsidiary of the Company ("ETC Entertainment"), and Mr. Lenfest; (iv) the Guaranty, dated April 24, 2009, by ETC Entertainment in favor of Mr. Lenfest; and (v) the Amended and Restated Open-End Mortgage and Security Agreement, dated April 24, 2009, by the Company in favor of Mr. Lenfest. These Agreements were entered into as part of, or directly related to, the 2009 Lenfest Financing Transaction. As part of the 2012 Financial Restructuring, the $10,000 in marketable securities associated with the Lenfest Pledge has been returned to Mr. Lenfest and the Lenfest Pledge has been terminated.

The warrants ETC issued to Mr. Lenfest as part of the 2009 Lenfest Financing Transaction were not terminated. See "Common Stock Warrants", below.

Preferred Stock

Presently, the Company has two classes of Cumulative Convertible Participating Preferred Stock authorized: Series D (11,000 shares authorized) and Series E (25,000 shares authorized) (together, the "Preferred Stock"). The Preferred Stock was authorized by the Board of Directors in April 2009 as part of the 2009 Lenfest Financing Transaction. The Preferred Stock has a par value of $0.05 per share and a stated value of $1,000 per share. The Preferred Stock is currently entitled to receive cumulative dividends at the rate of four percent (4%) per year in preference to the holders of the Company's Common Stock with respect to dividends. These dividends are payable only upon a liquidation event or when otherwise declared by the Board of Directors of the Company. The Company cannot declare or pay any dividends on its Common Stock until the dividends on the Preferred Stock have been paid. The Preferred Stock holders are entitled to receive any dividends paid with respect to the Common Stock on an "as-converted" basis. The Preferred Stock may be converted by the holder at any time and from time to time into the Company's Common Stock by dividing the stated value of the Preferred Stock by the conversion price established at the time of issuance (see Series D Preferred Stock and Series E Preferred Stock, below). Upon a liquidation event, the holders of the Preferred Stock would be entitled to participate in any proceeds in preference to any Common Stock holders. The Preferred Stock would also participate in any liquidation event with the Common Stock holders on an "as-converted" basis. The Preferred Stock conversion price is subject to adjustment for certain transactions including stock splits and issuance of equity securities below the conversion prices.

The Company has reviewed the accounting principles generally accepted in the United States of America applicable to the Preferred Stock; specifically, the Company has reviewed both ASC 480 – Distinguishing Liabilities from Equity and ASC 815 – Derivatives and Hedging. Upon its review, the Company determined that the Preferred Stock is within the control of the Company and that the attributes of the Preferred Stock are more akin to equity than debt. The specific attributes considered by the Company include the designation of the instruments, the conversion of the instruments to the Company's Common Stock, the participation feature, the non-mandatory conversion, the voting rights, and the ability to appoint directors. Secondly, the Company determined that the Preferred Stock qualifies as permanent equity because the Preferred Stock is not mandatorily redeemable, and there is no obligation to either repurchase the instruments or issue a variable amount of common shares. Lastly, the Company determined that the conversion feature qualifies for the scope exception of ASC 815 – Derivatives and Hedging as it is clearly and closely related to the Preferred Stock instrument.

Due to the Company's accumulated deficit as of February 24, 2012, all dividends accruing through this date for the Series D and Series E Preferred Stock issuances were recorded in the accompanying financial statements as a reduction in additional paid-in capital. During the current fiscal year, the Company entered into a position of retained earnings; thus, all $1,511 of dividends recorded during fiscal 2013 have been recorded as a reduction to retained earnings.

Issuances of the Preferred Stock are as follows:

Series D Preferred Stock

On September 28, 2012, as part of the 2012 Financial Restructuring and immediately following the closing of the Loan Agreement with PNC Bank, the Company purchased from Mr. Lenfest, at the stated price of $1,000 per share, 386 shares of Series D Preferred Stock, representing all of the Company's issued and outstanding shares of Series D Preferred Stock. Since there were no outstanding shares of Series D Preferred Stock for the period September 28, 2012 through February 22, 2013, there were no dividends accrued during this period. All Series D Preferred Stock dividends accrued as of September 28, 2012, which totaled $13 and represented dividends accrued during the period May 26, 2012 through September 28, 2012, were paid in cash subsequent to November 23, 2012; $10 was paid in December 2012 and $3 was paid in April 2013.

Series E Preferred Stock

On July 2, 2009, the Company issued 23,741 shares of Series E Preferred Stock to Mr. Lenfest in connection with the 2009 Lenfest Financing Transaction. The shares of Series E Preferred Stock are convertible to Common Stock at a conversion price per share equal to $2.00 and would have converted into 11,870,391 shares of the Company's Common Stock.

On March 10, 2010, August 12, 2010, and February 9, 2011, ETC entered into three separate agreements with Mr. Lenfest to repurchase and retire a total of 2,000 shares of Series E Preferred Stock owned by Mr. Lenfest. In the three agreements, the repurchases were made at the stated price of $1,000 per share for a total of $2,000.

On September 28, 2012, as part of the 2012 Financial Restructuring and immediately following the closing of the Loan Agreement with PNC Bank, the Company purchased from Mr. Lenfest, at the stated price of $1,000 per share, 9,614 shares of Series E Preferred Stock, representing a significant portion of the Company's issued and outstanding Series E Preferred Stock. Mr. Lenfest is the only holder of the outstanding Series E Preferred Stock, and 12,127 shares of Series E Preferred Stock remain outstanding as of February 22, 2013.

As of February 22, 2013, the Series E Preferred Stock totaled $12,127 and was convertible into 6,063,321 shares of the Company's Common Stock. All Series E Preferred Stock dividends accrued as of February 22, 2013, which totaled $404, were paid in cash in April 2013.

Common Stock Warrants

On February 28, 2009, in connection with a $2,000 loan made by Mr. Lenfest to the Company, the Company issued to Mr. Lenfest warrants to purchase 143,885 shares of ETC Common Stock, which shares were equal in value to ten percent (10%) of the $2,000 note. The warrants are exercisable for seven years following issuance at an exercise price of $1.39, which price equaled the average closing price of ETC Common Stock during the 120 days prior to the issuance of the warrant.

On July 2, 2009, in consideration of Mr. Lenfest's agreement to guarantee the $5,000 increase to the 2007 PNC Credit Facility, ETC issued to Mr. Lenfest warrants to purchase 450,450 shares of ETC Common Stock, which shares were equal in value to ten percent (10%) of the amount of the $5,000 increase. The warrants are exercisable for seven years following issuance at an exercise price per share equal to $1.11, equaling the average closing price of ETC Common Stock during the 120 days preceding the issuance of the warrant.

On January 4, 2011, the Company entered into amendments to each of the warrants issued to Mr. Lenfest pursuant to which Mr. Lenfest agreed to remove a provision in each of the warrants which provided anti-dilution protection in the event the Company issued securities at a price below the exercise price set forth in the warrants.

Dedicated Line of Credit Agreement with PNC Bank

The Company has a Dedicated Line of Credit in the amount of $5,422 with PNC Bank. The Company uses the Dedicated Line of Credit to satisfy performance bond and repayment guarantee requirements for an international contract. Use of this Dedicated Line of Credit is restricted to funding contract performance and repayment guarantee requirements under this specific contract.

As security for the Dedicated Line of Credit, the Company has deposited $5,422 in a certificate of deposit with PNC Bank. ETC is obligated to pay a fee of three percent (3%) per year for the Dedicated Line of Credit.

On March 8, 2013, the Company made an accelerated payment on the Term Loan in the amount of $1,181 with cash received from a partial reduction in its certificate of deposit securing the Dedicated Line of Credit. The certificate of deposit was able to be reduced in conjunction with the reduction of a Repayment Guarantee Bond associated with one of our international contracts for multiple Aerospace products. See Note 15 – Subsequent Events for additional details.

Export Import Committed Line of Credit Agreement with PNC Bank

On December 19, 2012, the Company entered into an Export Import Loan Agreement through PNC Bank, whereby the Company has an Ex-Im Line of Credit through which it may borrow against eligible export inventory and eligible export accounts receivable up to a maximum of $2,000. The agreement expires on October 31, 2015. Interest on advances under the agreement will be at the PNC Daily LIBOR Rate plus 2.50% (currently 2.70%). The agreement includes covenants that are generally consistent with its Line of Credit with PNC Bank. As of February 22, 2013, $600 was borrowed under the Ex-Im Line of Credit.

ETC-PZL Line of Credit Agreement

As of August 24, 2012, ETC-PZL had a line of credit in the amount of $175 with a Warsaw bank to fund current activity. The line of credit would have expired in July 2013. On November 20, 2012, this line of credit was increased to $1,125 and extended to November 2013. As of February 22, 2013, there were no outstanding borrowings under this line of credit ("ETC-PZL Line of Credit").

Summary of Long-Term Debt Obligations

Long-term debt obligations consist of the following as of:

	February 22, 2013	February 24, 2012
Credit facility payable to bank	$ 7,585	$ 16,716
Term loan	14,000	-
Borrowed under Ex-Im Line of Credit	600	-
Equipment lease	-	8
Total long-term debt obligations	22,185	16,724
Less: current portion of long-term debt obligations	(3,600)	(8)
Total long-term debt obligations, less current portion	**$ 18,585**	**$ 16,716**

The amounts of future long-term debt obligations maturing in each of the next five (5) fiscal years are as follows:

Fiscal Year	**Amount**
Fiscal 2014	$ 3,600
Fiscal 2015	3,000
Fiscal 2016	10,585
Fiscal 2017	3,000
Fiscal 2018	2,000
Total future long-term debt obligations	**$ 22,185**

7. Leases

Operating Leases

The Company leases certain premises and office equipment under operating leases, which expire over the next five (5) years. Future minimum rental payments required under non-cancelable operating leases having a remaining term expiring after one fiscal year as of February 22, 2013 are $378 in fiscal 2014; $309 in fiscal 2015; $302 in fiscal 2016; $100 in fiscal 2017; and $60 in fiscal 2018 and beyond. Total rental expense for all operating leases for fiscal 2013 and fiscal 2012 was $382 and $338, respectively.

8. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes, as well as the valuation of net loss carryforwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the potential realization of the related deferred tax asset.

As of February 22, 2013, the Company reviewed the components of its deferred tax assets and determined, based upon all available information, that its current and expected future operating income will more likely than not result in the realization of its deferred tax assets relating to its federal net operating loss carryforwards; all foreign net operating loss carryforwards available as of February 22, 2013 have been fully reserved. The Company has a net deferred tax asset related primarily to its federal net operating loss carryforwards of $4,812. Income tax provisions of $3,859 and $2,620 were recorded in fiscal 2013 and fiscal 2012, respectively.

As of February 22, 2013, the Company had approximately $13,590 of federal net loss carry forwards available to offset future income tax liabilities, which will begin to expire in 2025. In addition, the Company has the ability to offset deferred tax assets against deferred tax liabilities created for such items as depreciation and amortization.

Income tax expense consists of the following:

	Fiscal year ended	
	February 22, 2013	February 24, 2012
Current tax expense:		
U.S. Federal	$ 172	$ 275
U.S. State	51	212
Foreign	131	767
Total current	**354**	**1,254**
Deferred tax expense:		
U.S. Federal	$ 3,361	$ 1,236
U.S. State	89	712
Foreign	55	(582)
Total deferred	**3,505**	**1,366**
Total income tax expense	**$ 3,859**	**$ 2,620**

Effective tax rates were 43.7% and 35.0% for fiscal 2013 and fiscal 2012, respectively. Our effective fiscal 2013 tax rate was higher than fiscal 2012 primarily due to a smaller reduction in tax expense related to the research and development credit.

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. The examination by the Internal Revenue Service for fiscal 2010 is now complete. The changes that were made did not affect the tax reported on the originally filed return. The Company is no longer subject to U.S. federal tax examinations by tax authorities for the fiscal years before 2010. ETC-PZL is no longer subject to tax examinations in Poland for tax periods prior to December 31, 2007; ETC-Europe is no longer subject to tax examinations in the United Kingdom for tax periods prior to fiscal 2011. We are, however, subject to examination in various other foreign and state jurisdictions for fiscal years 2003-2013. We believe appropriate provisions for all outstanding tax issues have been made for all jurisdictions and all open years.

Significant components of our net deferred tax assets are as follows:

	February 22, 2013	February 24, 2012
Deferred tax assets:		
Net operating loss and credits	$ 7,179	$ 10,010
Foreign	375	610
Vacation accrual	211	203
Inventory reserve	412	427
Receivable reserve	145	147
Warranty reserve	51	63
Compensation and other reserves	193	177
Other, net	104	251
	8,669	11,888
Valuation allowance	(496)	(406)
Total deferred tax assets	**8,173**	**11,482**
Deferred tax liabilities:		
Depreciation	2,974	2,708
Amortization of capitalized software	173	283
Foreign	95	131
APB 23 liability	119	-
Total deferred tax liabilities	**3,361**	**3,122**
Total net deferred tax assets	**$ 4,812**	**$ 8,360**

As of February 22, 2013, we have provided for U.S. deferred income taxes and foreign withholding tax in the amount of $119 for all undistributed earnings not considered permanently reinvested in our non-U.S. subsidiaries since during fiscal 2013 our non-U.S. subsidiaries entered into a position of earnings and profit. As of February 24, 2012, there was no such provision for U.S. deferred income taxes or foreign withholding tax on any undistributed earnings in our non-U.S. subsidiaries since there were no such earnings as of February 24, 2012.

As of February 22, 2013, the amounts accrued for the payment of income tax-related interest and penalties included in the consolidated financial statements were as follows: interest of $34 and penalties of $72. As of February 24, 2012, the amounts accrued for the payment of income tax-related interest and penalties included in the consolidated financial statements were as follows: interest of $27 and penalties of $59.

As of February 22, 2013 and February 24, 2012, the total amount of unrecognized tax benefits was $715 and $668, respectively. These amounts, which are recorded on the Company's balance sheet within other accrued liabilities, are primarily associated with U.S. federal tax issues such as the amount of research and development tax credits claimed and taxation of foreign earnings. Income tax expense related to the recording of unrecognized tax benefits totaled $47 and $524 in fiscal 2013 and fiscal 2012, respectively.

9. Business Segment Information

We operate in two primary business segments, Aerospace and CIS. Aerospace encompasses the design, manufacture, and sale of: (i) Aircrew Training Systems; (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); and (iv) ADMS, as well as integrated logistics support for customers who purchase these products or similar products manufactured by other parties. These products and services provide customers with an offering of comprehensive solutions for improved readiness and reduced operational costs. Sales of our Aerospace products are made principally to U.S. and foreign government agencies. CIS encompasses the design, manufacture, and sale of: (i) steam and gas (ethylene oxide) sterilizers; (ii) environmental testing and simulation devices; and (iii) hyperbaric (100% oxygen) chambers for one person (monoplace chambers), as well as parts and service support for customers who purchase these products or similar products manufactured by other parties. Sales of our CIS products are made principally to the healthcare, pharmaceutical, and automotive industries.

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, and income taxes have been excluded from the determination of the total profit for segments. For presentation purposes, income, expenses, and assets not specifically identifiable to an individual business group or applicable to all groups and general corporate expenses, primarily central administrative office expenses, are reflected in the Corporate category. Property, plant, and equipment associated with the Company's NASTAR Center are included in the Aerospace segment; the remaining property, plant, and equipment are not identified with specific business segments because most of these assets are used in each of the segments.

In both fiscal 2013 and fiscal 2012, International sales totaling at least $500 were made to customers in eight (8) different countries. 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.

In fiscal 2013, two customers, (one U.S. defense agency and one international customer), each in the Aerospace segment, represented 10.0% or more of total net sales, and sales to these two customers totaling $29,926 represented 47.7% of total net sales. In fiscal 2012, three customers, (two U.S. defense agencies and one international customer), each in the Aerospace segment, represented 10.0% or more of total net sales, and sales to these three customers totaling $37,818 represented 57.0% of total net sales.

Included in the segment information for fiscal 2013 and fiscal 2012 are export sales of $21,507 and $22,478, respectively. Sales to the U.S. Government and its agencies aggregated to $22,217 and $27,181 for fiscal 2013 and fiscal 2012, respectively.

The following segment information reflects the accrual basis of accounting:

	Aerospace	CIS	Corporate	Company Total
Fiscal 2013:				
Net sales	$ 42,296	$ 20,477	$ -	$ 62,773
Interest expense, net	677	328	-	1,005
Depreciation and amortization	1,264	527	52	1,843
Operating income (loss)	9,121	3,887	(3,064)	9,944
Provision for income taxes	-	-	3,859	3,859
Identifiable assets	36,713	7,700	16,155	60,568
Expenditures for segment assets	1,006	73	225	1,304
Fiscal 2012:				
Net sales	$ 48,901	$ 17,393	$ -	$ 66,294
Interest expense, net	541	193	-	734
Depreciation and amortization	1,176	515	69	1,760
Operating income (loss)	7,197	4,058	(3,118)	8,137
Provision for income taxes	-	-	2,620	2,620
Identifiable assets	40,046	8,315	19,425	67,786
Expenditures for segment assets	1,670	304	170	2,144

Reconciliation to consolidated net income attributable to Environmental Tectonics Corporation:

	Fiscal 2013	Fiscal 2012
Operating income	$ 9,944	$ 8,137
Interest expense, net	(1,005)	(734)
Other (expense) income, net	(118)	85
Provision for income taxes	(3,859)	(2,620)
(Income) expense attributable to non-controlling interest	(14)	5
Net income attributable to Environmental Tectonics Corporation	**$ 4,948**	**$ 4,873**

10. Stock Option Plans

The following is a summary of the status of the Company's Stock Option Plans:

	Fiscal year ended			
	February 22, 2013		February 24, 2012	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding at beginning of year	270,921	$ 4.35	260,921	$ 4.44
Granted	-	$ -	10,000	$ 2.00
Exercised	-	$ -	-	$ -
Forfeited	(51,004)	$ 4.90	-	$ -
Outstanding at end of year	219,917	$ 4.23	270,921	$ 4.35
Options exercisable at year end	213,250		223,254	
Weighted average fair value of options granted during the year		$ -		$ 0.89

The following information applies to options outstanding as of February 22, 2013:

	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding as of February, 22 2013	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable at February 22, 2013	Weighted average exercise price
Less than $2.64	111,500	6.97	$2.58	104,833	$2.62
$5.12	50,000	3.02	$5.12	50,000	$5.12
$6.07 to $7.24	58,417	2.66	$6.60	58,417	$6.60
Total	**219,917**			**213,250**	

The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model. There were no options granted in fiscal 2013; there were 10,000 options granted in fiscal 2012.

The cost for stock option compensation was $69 and $101 in fiscal 2013 and fiscal 2012, respectively. As of February 22, 2013, there were 58,417 options outstanding under the 1998 Incentive Stock Option Plan, which expired in August 2008.

As of February 22, 2013, the Company had two stock-based compensation plans:

Employee, Director and Consultant Stock Plan

In July 2009, the Company adopted the 2009 Employee, Director and Consultant Stock Plan. This Plan authorizes the Board of Directors (or a committee appointed under the Board of Directors) to grant option awards for the purchase of Common Stock or Common Stock awards of up to 1,000,000 shares of Common Stock to employees, officers, directors, consultants, and advisors of the Company and its Subsidiaries. The Plan allows for the establishment of an exercise price at the time each option is granted. The exercise price shall not be less than the fair market value, or in the case of a ten percent (10%) owner, one-hundred and ten percent (110%), of a share of the Company's Common Stock on the date of grant of such option. The plan also allows the Board of Directors or its appointed committee to establish the exercise period(s) of any option awards. Granted options have a maximum term of ten (10) years. This Plan was approved by the shareholders on July 2, 2009. As of February 22, 2013, there were 888,500 shares available to be granted under this Plan.

Non-employee Director Stock Plan

In September 2005, the Company adopted a stock option plan which allows for the granting to non-employee members of the Board of Directors of options to purchase up to 600,000 shares of Common Stock. The Plan provides that the exercise price shall not be less than one-hundred percent (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 ten (10) years. The Plan shall remain in effect until terminated by the Board of Directors. As of February 22, 2013, there were 550,000 shares available to be granted under this Plan.

11. Other Related Party Transactions

ETC purchases industrial products from Industrial Instruments and Supplies, Inc. ("Industrial Instruments"), which is owned by Christine and Charles Walter, the daughter and son-in-law of William F. Mitchell, ETC's President and Chief Executive Officer ("Mr. Mitchell"). During fiscal 2013 and fiscal 2012, the Company purchased $668 and $634, respectively, from Industrial Instruments. As of February 22, 2013, ETC owed $173 to Industrial Instruments. ETC also rents office space to Industrial Instruments at ETC's corporate headquarters. During both fiscal 2013 and fiscal 2012, Industrial Instruments paid to ETC rent in the amounts of $8.

ETC purchases travel accommodations from Jet Set Travels, a company that employs Kathleen Mahon, the daughter of Mr. Mitchell. During fiscal 2013 and fiscal 2012, ETC purchased travel through Jet Set Travels totaling $478 and $421, respectively, and Ms. Mahon received approximately $25 in fiscal 2013 and $22 in fiscal 2012 from her employer in commissions on account of such purchases. Ms. Mahon is also engaged by ETC as a consultant to review expense reports submitted by Company employees. During both fiscal 2013 and fiscal 2012, Ms. Mahon received $20 in consideration for such services.

ETC employs William F. Mitchell, Jr., the son of Mr. Mitchell, as its Vice President, Contracts/Purchasing, and David Mitchell, the son of Mr. Mitchell, as its Business Unit Manager of ETC Sterilization Systems. In fiscal 2013, Mr. William F. Mitchell, Jr. received $183 and Mr. David Mitchell received $187 in compensation from ETC. In fiscal 2012, Mr. William F. Mitchell, Jr. received $175 and Mr. David Mitchell received $211 in compensation from ETC.

ETC uses two properties owned by Mr. Mitchell. During both fiscal 2013 and fiscal 2012, ETC paid $60 to Mr. Mitchell in connection with ETC's use of these properties.

12. Commitments and Contingencies

There are no material pending legal proceedings to which ETC or any of its subsidiaries is a party or of which any of their property is the subject.

Other Matters

Certain other claims, suits, and complaints arising in the ordinary course of business have been filed or are pending against us. We believe, after consultation with legal counsel handling these specific matters, 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 be expected to have a significant effect on our financial position or results of operations if determined adversely against us.

13. Employee Benefit Plans

The Company maintains a 401(k) retirement savings plan for eligible employees. The Company historically contributed one-hundred percent (100%) to the plan based on the first four percent (4%) of the employees' qualifying contributions; however, effective January 1, 2013, the Company now contributes one-hundred percent (100%) to the plan based on the first four percent (4%) of the employees' qualifying contributions plus an additional fifty percent (50%) of the next two percent (2%) of the employees' qualifying contributions. The Company's contributions totaled $451 and $422 in fiscal 2013 and fiscal 2012, respectively.

The Company had an Employee Stock Purchase Plan, which was originally adopted by the Board of Directors on November 3, 1987, but was subsequently terminated by the Board of Directors effective January 1, 2013. The Company originally reserved 270,000 shares for issuance under this plan, of which 163,406 shares were still remaining as of the effective termination date of January 1, 2013.

14. Fair Value Measurements and Interest Rate Swap

Our assets and liabilities that are measured at fair value on a recurring basis include the unrealized gains or losses on interest rate swap contracts. We use significant other observable market data or assumptions (Level 2 inputs as defined in the accounting guidance) that we believe market participants would use in pricing similar assets or liabilities, including assumptions about counterparty risk. Our fair value estimates reflect an income approach based on the terms of the interest rate contracts and inputs corroborated by observable market data including interest rate curves.

As of February 22, 2013, we had one interest rate swap contract in place to reduce our exposure to fluctuations in interest rates on our Term Loan. The swap converts the variable interest rate to a fixed interest rate initially on $5,000 of our $15,000 Term Loan. The effective date of the interest rate swap was September 28, 2012, and it is scheduled to expire on September 28, 2017. The notional amount of $5,000 will decrease ratably over the duration of the interest rate swap agreement. The interest rate swap effectively fixes our LIBOR interest rate on the notional amount at a rate of 0.74% in excess of the margin. We have recognized the fair value of our interest rate swap as a long-term liability of approximately $28 as of February 22, 2013.

We recognize any differences between the variable interest rate payments and the fixed interest rate settlements from our swap counterparty as an adjustment to interest expense over the life of the swap. We have designated the swap as a cash flow hedge and we record the changes in the estimated fair value of the swap to accumulated other comprehensive loss. If our interest rate swap became ineffective, we would immediately recognize the change in the estimated fair value of our swap in earnings. Since inception, we have not recognized any gains or losses on these swaps through income and there has been no effect on income from hedge ineffectiveness.

Failure of our swap counterparty would result in the loss of any potential benefit to us under our swap contracts. In this case, we would still be obligated to pay the variable interest payments underlying the Term Loan. Additionally, failure of our swap counterparty would not eliminate our obligation to continue to make payments under our existing swap contract if we continue to be in a net pay position.

15.Subsequent Events

The Company has evaluated subsequent events through May 23, 2013, the date of issuance of its consolidated financial statements and determined that there were no material subsequent events other than disclosed below requiring adjustment to, or disclosure in, the consolidate financial statements for the year ended February 22, 2013.

On March 8, 2013, the Company made an accelerated payment on the Term Loan in the amount of $1,181 with cash received from a partial reduction in its certificate of deposit securing the Dedicated Line of Credit in the amount of $5,422 with PNC Bank. The certificate of deposit was able to be reduced in conjunction with the reduction of a Repayment Guarantee Bond associated with one of our international contracts for multiple Aerospace products.

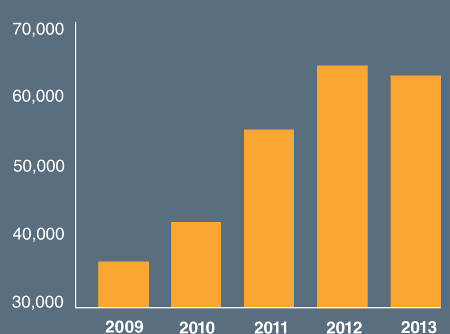
On April 9, 2013, the Company entered into an amendment to the September 28, 2012 Loan Agreement pursuant to which PNC Bank is extending to ETC a $15,000 revolving line of credit and a $15,000 term loan. The amendment provides an enhanced investment and borrowing sweep feature that allows ETC to increase returns on idle cash balances and minimize interest expense on the Company's Line of Credit. With the sweep feature, excess cash in ETC's checking account is invested and automatically liquidated as needed to cover daily transactions. Effective as of the date of this amendment, the interest rate on the Line of Credit Note (currently 2.70%) will be based on the PNC Daily LIBOR Rate plus a margin of 2.25% to 2.75% depending on the Operating Leverage Ratio (currently 2.50%).

QUALITY THROUGH
INTEGRITY AND TECHNOLOGY

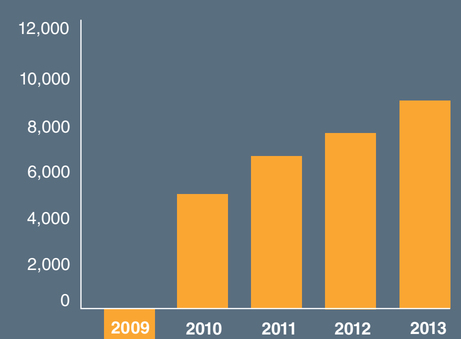
FIVE YEAR SUMMARY

(in thousands, except per share information)	Fiscal 2009	Fiscal 2010	Fiscal 2011	Fiscal 2012	Fiscal 2013
Net sales	$ 36,687	$ 42,271	$ 55,451	$ 66,294	$ 62,773
Gross profit	11,858	18,824	21,790	23,531	24,869
Gross profit margin %	*32.3%*	*44.5%*	*39.3%*	*35.5%*	*39.6%*
Operating (expense) income	(346)	6,600	8,290	8,137	9,944
Operating margin %	*(0.9%)*	*15.6%*	*15.0%*	*12.3%*	*15.8%*
(Expense) income before income taxes	(1,982)	4,630	6,877	7,488	8,821
Pre-tax income margin %	*(5.4%)*	*11.0%*	*12.4%*	*11.3%*	*14.1%*
Income tax (benefit) provision	-	(1,819)	(7,665)	2,620	3,859
Net (loss) income	(1,982)	6,449	14,542	4,868	4,962
Expense (income) attributable to non-controlling interest	8	4	(8)	5	(14)
Net (loss) income attributable to ETC	(1,974)	6,453	14,534	4,873	4,948
Preferred Stock dividends	(927)	(1,885)	(2,278)	(2,208)	(1,511)
(Expense) income attributable to common and participating shareholders	$ (2,901)	$ 4,568	$ 12,256	$ 2,665	$ 3,437
Diluted earnings per share	$ (0.32)	$ 0.26	$ 0.59	$ 0.13	$ 0.19
Working capital	$ 4,684	$ 15,326	$ 20,242	$ 27,786	$ 25,135
Total long-term debt obligations	22,081	10,093	3,303	16,724	22,185
Total assets	37,278	51,729	54,051	67,786	60,568
Total shareholders' (deficiency) equity	(11,710)	17,414	28,129	30,825	24,219
Capital expenditures	1,908	1,824	865	2,144	1,304
Depreciation and amortization	1,797	1,309	1,354	1,760	1,843
Interest expense, net	1,569	1,308	824	734	1,005
EBITDA	**$ 1,384**	**$ 7,247**	**$ 9,055**	**$ 9,982**	**$ 11,669**

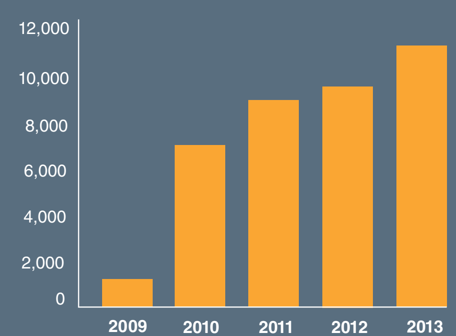
NET SALES
(in thousands of dollars)



PRE-TAX INCOME
(in thousands of dollars)



EBITDA
(in thousands of dollars)



Company Affiliates and Locations

The consolidated financial statements include the accounts of ETC, our 95%-owned subsidiary ETC-PZL, and our 99%-owned subsidiary ETC-Europe. ETC does not have any unconsolidated legal entities, “special purpose” entities, or off-balance sheet arrangements. As of February 22, 2013, we had 336 full-time employees (the same number of employees as of February 24, 2012), of which 5 were employed in executive positions, 151 were engineers, engineering designers, or draftspersons, 76 were administrative (sales, sales support, accounting, or general administrative) or clerical personnel, and 104 were engaged principally in production, operations, or field support. A total of 166 employees were stationed in Southampton, Pennsylvania, a northern suburb of Philadelphia, Pennsylvania.

We are an ISO 9001 certified manufacturer. We are also ISO 13485 certified for our medical devices. We operate in five major locations consisting of manufacturing facilities, product development, and administration. A summary of square footage and use is presented below:

Location	Approximate Square Footage	Function	Owned/Leased	Segment
Southampton, Pennsylvania	92,000	Manufacturing (64,000 sq. ft), NASTAR Center (22,000 sq. ft.), and Corporate Headquarters (6,000 sq. ft.)	Owned	Aerospace CIS
Southampton, Pennsylvania	15,000	Service and spare parts warehouse	Leased	CIS
Orlando, Florida	8,700	Product development and administration	Leased	Aerospace
Warsaw, Poland	28,000	Manufacturing, product development, and administration	Leased	Aerospace
Ankara, Turkey	5,700	Software development	Leased	Aerospace CIS
Total	**149,400**			

The NASTAR Center, which is included in the Company’s Southampton, Pennsylvania owned property, includes the following aerospace training and research equipment:

- ATFS-400-25 PHOENIX High Performance Human Centrifuge;
- GYROLAB GL-1500 Advanced Spatial Disorientation Trainer;
- Altitude (Hypobaric) Chamber;
- Ejection Seat Simulator; and
- Night Vision Training System and Night Vision Goggle Training System.

Corporate Governance

The Board of Directors is comprised of eight (8) members, six (6) of whom who are considered “independent” directors (not an employee, not affiliated with the Company’s auditors, and not part of an interlocking directorate). Directors are nominated based on their individual qualifications and experience, the overall balance of the Board of Directors’ background and experience, and each individual’s willingness to fulfill their obligations and to contribute appropriately.

The Board of Directors meets four times per year in addition to various Board committee meetings held throughout the year. Standing committees consist of the Audit Committee, the Compensation Committee, and the Nominating and Governance Committee. These committees each have defined charters that address the committees’ purpose, goals, and responsibilities. All committees meet on a scheduled basis. Please refer to the Investors section of our website (www.etcusa.com) for more information on corporate governance.

	Audit Committee	Compensation Committee	Nominating and Governance Committee
George K. Anderson, M.D.		Member	Chairperson
George A. Sawyer	Member	Chairperson	
Winston E. Scott		Member	Member
Linda J. Brent Ed.D	Member		Member
Roger Colley	Chairperson	Member	
Michael D. Malone	Member	Member	

Reporting Requirements

The Company is not currently required to register with the SEC and therefore is not subject to the reporting requirements of a public company; however, the Company issues periodic press releases, quarterly unaudited statements and an annual report with audited financial statements.

Interim Consolidated Financial Statements

Interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto for fiscal 2013. The results for any interim period are not necessarily indicative of results for the full year. Certain information and footnote disclosures normally included in audited financial statements have been omitted. As mentioned previously, the Company is not subject to SEC reporting requirements and therefore its quarterly interim consolidated financial statements are not subject to an interim review by Independent Auditors as prescribed by the SEC.

Investor and Shareholder Information

Shareholder Inquiries

Questions concerning your account, address changes, consolidation of duplicate accounts, lost certificates, and other related matters should be addressed to ETC's transfer agent:

American Stock Transfer & Trust Company, LLC
6201 15th Avenue
Brooklyn, NY 11219
Toll Free: +1.800.937.5449
Telephone: +1.718.921.8124
Website: www.amstock.com

Stock Exchange Listing

The Common Stock of ETC is traded under the symbol "ETCC" on the electronic Pink Sheets and is listed by the OTC Markets Group, Inc., reporting service for over-the-counter stocks. Stock quotation information is available through stock reporting services on the Internet at www.otcmarkets.com.

Corporate Data

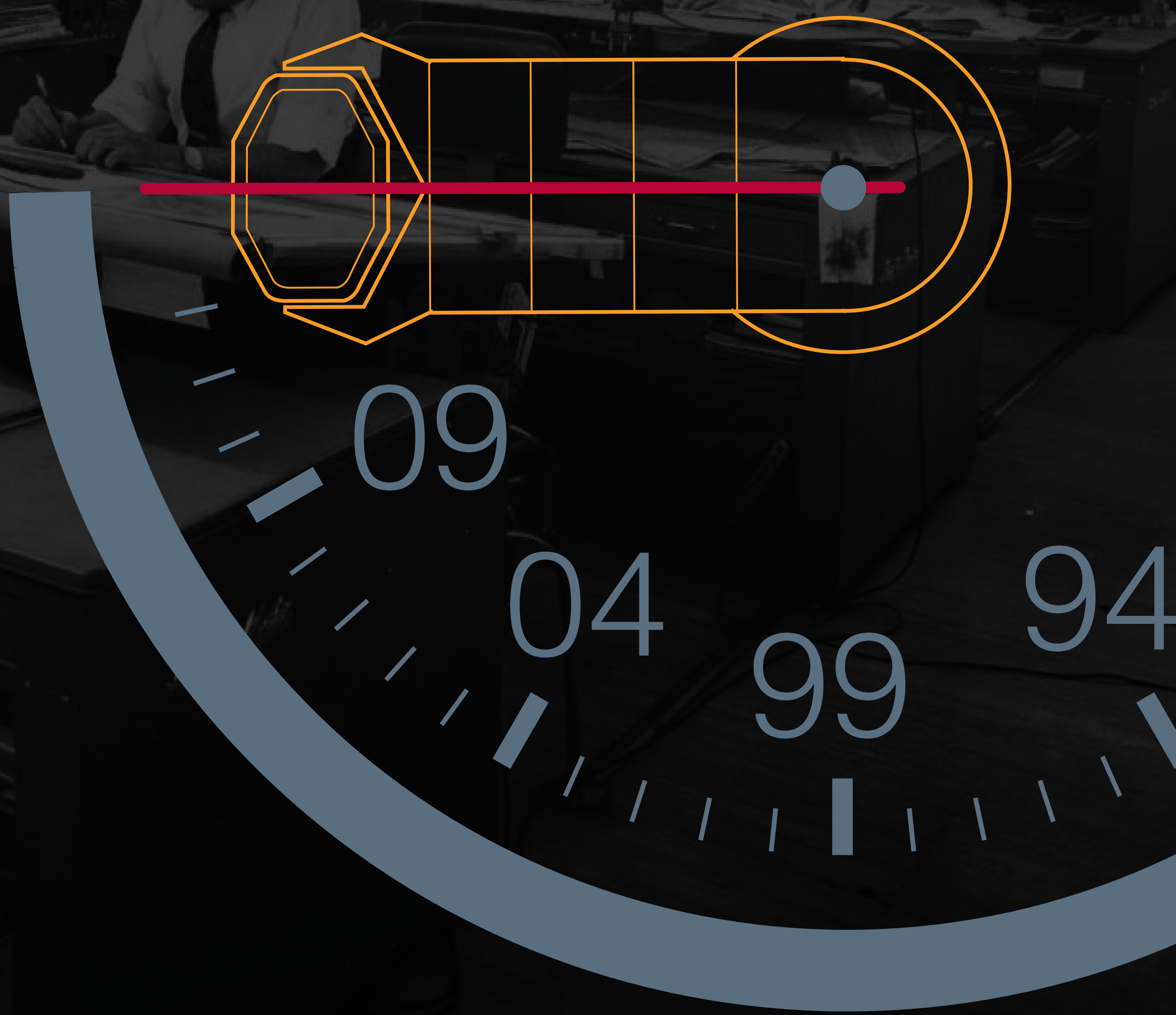
Environmental Tectonics Corporation
125 James Way, Southampton, Pa. 18966

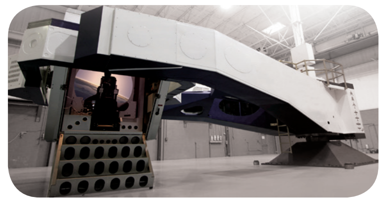
For further information, contact:
Robert L. Laurent, Jr.,
Chief Financial Officer.
Telephone: +1.215.355.9100 x1550

You can access Company information including press releases, earnings announcements, history and other information through the Internet by visiting the ETC website at www.etcusa.com.

OVER 40 YEARS OF SIMULATION

Since our founding in 1969, ETC's diverse product line has grown to include hyperbaric chambers, sterilizers, human centrifuges, ejection seat trainers, night vision trainers, and disorientation trainers. The common thread across all ETC's products is world-class technology and engineering.





ETC Aircrew Training Systems (ATS)
For over four decades, ATS has provided clients in over 80 countries with simulation systems designed for high–G, SD, SA, aircraft egress, night vision, hypoxic environment, tactical aviation, avionics maintenance, helicopter flight and water survival training and research applications. *(www.etcaircrewtraining.com)*

ETC Sterilization Systems
Specializing in medium to large (30 to 6000 cu. ft.) EO and steam sterilizers, ETC Sterilization Systems serves the pharmaceutical, biotech, medical device and life sciences market with unique design solutions for any challenge. *(www.etcsterilization.com)*

The National Aerospace Training and Research (NASTAR) Center
The National AeroSpace Training And Research (NASTAR) Center (est. 2007) is the premier commercial air and space training, research and educational facility. It combines state-of-the-art flight simulation with physiology-based courseware to optimize human performance in extreme environments. *(www.NASTARcenter.com)*

ETC Testing and Simulation Systems (TSS)
TSS has designed, manufactured and installed state-of-the-art environmental simulation systems for the automotive-testing and HVAC industries since 1969. Offering a complete line of industry-leading test equipment developed for clients' individual needs, TSS offers the most customized equipment available for optimizing R&D, test and validation programs. *(www.testingandsimulation.com)*

ETC Simulation
ETC Simulation's flagship product is the Advanced Disaster Management Simulator (ADMS), a realistic, virtual emergency management simulation training system. Based in Orlando, Fla., ETC Simulation offers the most thorough training for incident command and disaster management teams at all levels. *(www.etcsimulation.com)*

ETC BioMedical Systems
Founded in 1971, ETC BioMedical Systems is the world's first provider of computer-driven HBOT chambers. Groundbreaking innovations include the O.S.C.A.R. computerized control system and our exclusive undercarriage gurney storage solution for optimized space. *(www.etchyperbaricchambers.com)*

ETC GLOBAL HEADQUARTERS

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