

ESCO TECHNOLOGIES INC
Form DEF 14A
December 22, 2004

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

**SCHEDULE 14A
(RULE 14a-101)**

**INFORMATION REQUIRED IN PROXY STATEMENT
SCHEDULE 14A INFORMATION**

**PROXY STATEMENT PURSUANT TO SECTION 14(a) OF THE SECURITIES
EXCHANGE ACT OF 1934 (AMENDMENT NO.)**

Filed by the registrant [X]

Filed by a party other than the registrant []

Check the appropriate box:

- [] Preliminary proxy statement [] Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
- [X] Definitive proxy statement
- [] Definitive additional materials
- [] Soliciting material pursuant to Rule 14a-12

ESCO TECHNOLOGIES INC.

(Name of Registrant as Specified in Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of filing fee (Check the appropriate box):

- [X] No fee required.
- [] Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.
- (1) Title of each class of securities to which transaction applies:

- (2) Aggregate number of securities to which transaction applies:

- (3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

- (4) Proposed maximum aggregate value of transaction:

- (5) Total fee paid:

- [] Fee paid previously with preliminary materials.

- [] Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the form or schedule and the date of its filing.

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(1) Amount previously paid:

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(3) Filing party:

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ESCO TECHNOLOGIES INC. AUDIT & FINANCE COMMITTEE CHARTER November 10, 2004

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**NOTICE OF THE ANNUAL MEETING OF
THE STOCKHOLDERS OF
ESCO TECHNOLOGIES INC.**

St. Louis, Missouri

December 22, 2004

TO THE STOCKHOLDERS OF
ESCO TECHNOLOGIES INC.:

The Annual Meeting of the Stockholders of ESCO Technologies Inc. will be held at the Company's offices located at 8888 Ladue Road, Suite 200, St. Louis County, Missouri 63124 on Thursday, February 3, 2005, commencing at 9:30 A.M. St. Louis time, at which meeting only holders of record of the Company's common stock at the close of business on December 6, 2004 will be entitled to vote, for the following purposes:

1. To elect three directors;
2. To vote on a proposal to ratify the Company's selection of KPMG LLP as independent auditors for the fiscal year ending September 30, 2005; and
3. To transact such other and further business, if any, as lawfully may be brought before the meeting.

ESCO TECHNOLOGIES INC.

BY
*Chairman and
Chief Executive Officer*

Secretary

Even though you may plan to attend the meeting in person, please execute the enclosed form of proxy and mail it promptly. A return envelope which requires no postage if mailed in the United States is enclosed for your convenience.

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ESCO TECHNOLOGIES INC.

8888 Ladue Road, St. Louis, Missouri 63124

PROXY STATEMENT

FOR THE ANNUAL MEETING OF THE STOCKHOLDERS TO BE HELD FEBRUARY 3, 2005

This proxy statement is furnished to the holders of all of the issued and outstanding shares of common stock (the **Common Shares**) of ESCO Technologies Inc. (the **Company**) in connection with the solicitation of proxies for use in connection with the Annual Meeting of the Stockholders to be held February 3, 2005, and all adjournments thereof, for the purposes set forth in the accompanying Notice of the Annual Meeting of the Stockholders. Such holders are hereinafter referred to as the **Stockholders**. The Company is first mailing this proxy statement and the enclosed form of proxy to Stockholders on or about December 22, 2004.

Whether or not you expect to be present in person at the meeting, you are requested to fill in, sign, date and return the enclosed form of proxy. If you attend the meeting, you may vote by ballot. If you do not attend the meeting, the Common Shares can be voted only when represented by a properly executed proxy. In this case you have several choices:

You may vote on each proposal when returning the enclosed proxy form, in which case the Common Shares will be voted in accordance with your choices.

You may, when appropriate, indicate a preference to abstain on any proposal, which will have the effect described in **VOTING** on page 19.

You may return a properly executed proxy form without indicating your preferences, in which case the proxies will vote the Common Shares FOR election of the directors nominated by the Board of Directors, and FOR the proposal to ratify the Company's selection of KPMG LLP as independent auditors for the fiscal year ending September 30, 2005, and in their discretion on such other business as may properly come before the meeting.

Any person giving such proxy has the right to revoke it at any time before it is voted by giving written notice of revocation to the Secretary of the Company, by duly executing and delivering a proxy bearing a later date, or by attending the Annual Meeting and casting a contrary vote in person.

The close of business on December 6, 2004 was fixed as the record date for the determination of the Stockholders entitled to vote at the Annual Meeting of the Stockholders. As of the record date, 12,915,791 Common Shares were outstanding and entitled to be voted at such meeting. The Stockholders will be entitled to cast one vote for each Common Share held of record on the record date.

A copy of the Company's Annual Report to Stockholders for the fiscal year ended September 30, 2004 accompanies this proxy statement.

The solicitation of this proxy is made by the Board of Directors of the Company. The solicitation will be by mail, and the expense thereof will be paid by the Company. Proxies may also be solicited by telephone, email or telefax by directors, officers or regular employees of the Company.

I. ELECTION OF DIRECTORS

The Board of Directors unanimously recommends a vote FOR election of W.S. Antle III, L.W. Solley and J.D. Woods, the three nominees for Directors listed below.

Nominees and Continuing Directors

The Company's Bylaws provide that the number of directors shall not be less than three nor greater than ten, and shall be determined from time to time by majority vote of the Board of Directors. In accordance with the Bylaws, the Board of Directors has fixed the number of directors at nine. The Board is divided into three

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classes, with the terms of office of each class ending in successive years. Three directors of the Company are to be elected for terms expiring at the Annual Meeting in 2008, or until their respective successors have been elected and have qualified. Currently, there is a total of eight directors. Pursuant to the Company's Articles of Incorporation, a majority of the directors in office may fill any vacancy on the Board of Directors. As of the date of mailing of this proxy statement, the Company has not determined whether or whom to propose as an additional director. Certain information with respect to the nominees for election as directors proposed by the Company and the other directors whose terms of office as directors will continue after the Annual Meeting is set forth below. Should any one or more of the nominees be unable or unwilling to serve (which is not expected), the proxies (except proxies marked to the contrary) will be voted for such other person or persons as the Board of Directors of the Company may recommend. Proxies cannot be voted for more than three nominees.

Name, Age, Principal Occupation or Position, Other Directorships	Served as Director Since
TO BE ELECTED FOR TERMS ENDING IN 2008	
W.S. Antle III, 60 Former Chairman, President and Chief Executive Officer of Oak Industries, Inc., manufacturer of engineered products for the telecommunications industry Director of John H. Harland Company, Checkpoint Systems, Inc. and Linc.net, Inc.	1994
L.W. Solley, 62 Retired Executive Vice President, Emerson Electric Co., manufacturer of electrical and other products	1999
J.D. Woods, 73 Retired Chairman and Chief Executive Officer, Baker Hughes Incorporated, supplier of oilfield equipment and services Director of Varco International Inc., OMI Corporation, United States Enrichment Corporation, Foster Wheeler Ltd. and Integrated Electrical Services, Inc.	2001
TO CONTINUE IN OFFICE UNTIL 2007	
V.L. Richey, Jr., 47 Chairman and Chief Executive Officer of the Company	2002
J.M. Stolze, 61 Vice President and Chief Financial Officer, Stereotaxis, Inc., manufacturer of medical instruments	1999
TO CONTINUE IN OFFICE UNTIL 2006	
C.J. Kretschmer, 48 President and Chief Operating Officer of the Company	2002
J.M. McConnell, 63 Retired President and Chief Executive Officer, Instron Corporation, manufacturer of scientific instruments	1996
D.C. Trauscht, 71 Chairman, BW Capital Corporation, private investment company Director of OMI Corporation, Bourns Inc., Integrated Electrical Services, Inc. and Recon Optical Inc.	1991

Each of the nominees and continuing directors has had the same position with the same employer as stated in the preceding table during the past five years, except as follows:

From May 1995 until January 2000, Mr. Antle was Chairman, President and Chief Executive Officer of Oak Industries, Inc.

From November 1992 until February 2002, Mr. Solley was Executive Vice President of Emerson Electric Co.

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From March 1998 until October 2000, Mr. Richey was Vice President of the Company, and was Senior Vice President and Group Executive from October 2000 to August 2001. Mr. Richey was President and Chief Operating Officer from August 2001 to October 2002. Since October 2002, he has been Chief Executive Officer of the Company, and since April 2003, he has also been Chairman.

From June 1995 until December 2003, Mr. Stolze was Executive Vice President and Chief Financial Officer of MEMC Electronic Materials, Inc. Since May 2004, he has been Vice President and Chief Financial Officer of Stereotaxis, Inc.

Mr. Kretschmer was Vice President and Chief Financial Officer of the Company from October 1999 until February 2001 and Senior Vice President and Chief Financial Officer from February 2001 to February 2002. Mr. Kretschmer was Executive Vice President and Chief Financial Officer from February 2002 to October 2002. Since the latter date, he has been President and Chief Operating Officer of the Company.

From April 1990 until December 2001, Mr. McConnell was President and Chief Executive Officer of Instron Corporation.

Board of Directors and Committees

The Board has determined that no non-employee director has any material relationship with the Company or its affiliates or any member of the senior management of the Company or his or her affiliates; that each such director meets the independence standards of the New York Stock Exchange; and that each non-employee director is deemed to be independent. The Board considered that Mr. Stolze is an officer of a company that purchased approximately \$40,000 of shielding products from a subsidiary of the Company in fiscal 2004, and determined that this transaction does not impact the independence of Mr. Stolze because it was on standard terms and conditions and was conducted at arms length. There were five meetings of the Board of Directors during fiscal year 2004. All of the incumbent directors attended at least 75% of the meetings of the Board and committees on which they served. The Company's policy requires the attendance of all directors at the Annual Meeting of Stockholders, except for absences due to causes beyond the reasonable control of the director. Each of the eight directors in office at the time of the 2004 Annual Meeting attended that meeting except Mr. Antle, who was unable to attend due to bad weather.

Directors who are employees of the Company do not receive any compensation for service as directors. Effective January 1, 2004, compensation paid to non-employee directors during fiscal 2004 was changed to the following: annual cash retainer for each non-employee director \$20,000; additional annual cash retainer for Lead Director \$15,000; annual fee for Board meetings \$6,000; annual cash retainer for Chairman of Audit and Finance Committee \$7,000; annual cash retainer for Chairmen of Human Resources and Compensation and Nominating and Corporate Governance Committees \$5,000; annual fee for meetings of Audit and Finance Committee and Human Resources and Compensation Committee \$4,800; annual fee for meetings of Nominating and Corporate Governance Committee \$6,000. In addition, in fiscal 2004 each non-employee director received a retainer of 325 Common Shares per quarter. As of January 1, 2005, the following changes to the foregoing will become effective: (i) the quarterly Common Shares retainer will be increased to 400 shares, and (ii) the fee for Board meetings will be reduced to \$4,800 to reflect a reduction in the number of Board meetings per year. All of the above-mentioned cash retainers and fees were, and will be, paid in advance in January of each year.

Under the Company's extended compensation plan for non-employee directors who began Board service prior to April 2001, each director currently on the Board who has served as a non-employee director for at least five years or whose tenure as a director expires pursuant to the Company's Bylaws restriction regarding maximum age for election will, after the later of termination of services as a director or reaching age 65, receive for life a percentage of the fiscal year 2001 annual cash retainer for directors. Such percentage ranges from 50% to 100% based upon years of service as a director. In the event of death of a retired director who is eligible under this plan, 50% of the benefit will be paid to the surviving spouse for life. On or after retirement, if the eligible director so elects, the actuarial equivalent of the benefit may be received in a single lump sum.

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Directors may elect to defer receipt of all of the cash portion and/or all of the stock portion of the quarterly retainer. If elected, the deferred amounts are credited to the director's deferred compensation account in stock equivalents. Deferred amounts will be distributed in Common Shares or cash at such future dates as specified by the director unless distribution is accelerated in certain circumstances, including a change in control of the Company. The stock portion which has been deferred may only be distributed in Common Shares.

CORPORATE GOVERNANCE

The Board of Directors has adopted corporate governance guidelines and a code of business conduct and ethics applicable to all of the Company's directors, officers and employees. These documents are posted on the Company's website: www.escotechnologies.com. A copy of each of the corporate governance guidelines and the code of business conduct and ethics is also available in print to any Stockholder who requests it.

Mr. Trauscht, the Company's Lead Director, presides at meetings of the non-employee directors, which occur on a regular basis. Interested parties who wish to make their concerns known to the Company's non-employee directors may communicate directly with the Lead Director by writing to: Mr. D.C. Trauscht, Lead Director, ESCO Technologies Inc., 8888 Ladue Road, Suite 200, St. Louis, MO 63124-2056.

COMMITTEES

The members of the Board of Directors are appointed to various committees. The standing committees of the Board are: the Executive Committee, the Audit and Finance Committee, the Human Resources and Compensation Committee and the Nominating and Corporate Governance Committee. Each of these committees operates under a written charter adopted by the Board of Directors.

The Executive Committee's function is to exercise the full authority of the Board of Directors between Board meetings, except that the Executive Committee may not take certain specified actions which the Board of Directors has reserved for action by the whole Board. The Committee held no meetings in fiscal year 2004. Mr. Richey (Chairman), Mr. Antle and Mr. Trauscht are the members of the Committee.

The Audit and Finance Committee's functions generally are to assist oversight by the Board of Directors of the Company's financial reporting process, the Company's compliance with legal and regulatory requirements, the independent auditors' qualifications and independence, and the performance of the Company's out-sourced internal audit function and independent auditors. These functions include the responsibility to appoint, retain and oversee the firm of independent auditors performing the annual audit; to annually evaluate the qualifications, independence and prior performance of the independent auditors; to review the scope of the auditors' work and approve their annual audit fees and their other non-audit service fees; to review the Company's internal controls with the independent auditors and the internal audit executive; to review with the independent auditors any problems they may have encountered during the annual audit; discuss 10-K and 10-Q with management and independent auditors before filing; review and discuss earnings press release; discuss with management major financial risk exposures; to review the annual plan and associated resource allocation of the out-sourced internal audit function; to review the Company's reports to Stockholders with management and the independent auditors and receive certain assurances from management; to prepare a report as required by the Securities and Exchange Commission to be included in the annual proxy statement; and to review the effectiveness of the Company's legal, regulatory and corporate governance compliance programs. Each member of Committee is an independent Director, as defined in the applicable listing standards of the New York Stock Exchange. The Board of Directors has determined that Mr. Stolze, a member of the Audit and Finance Committee, is an audit committee financial expert within the meaning of Item 401(h) of Regulation S-K under the Securities Exchange Act of 1934, as amended (the Exchange Act), and is independent within the meaning of Item 7(d)(3)(iv) of Schedule 14A under the Exchange Act. The Committee met eight times in fiscal year 2004. Mr. Antle (Chairman), Mr. McConnell and Mr. Stolze are the members of the Committee. The Committee's charter (Appendix A to this Proxy Statement) is

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posted on the Company's website: www.escotechnologies.com and is available in print to any Stockholder who requests it.

The Human Resources and Compensation Committee's functions generally are to review and approve corporate goals and objectives relevant to compensation of the Chief Executive Officer; to evaluate the Chief Executive Officer's performance in light of these goals and objectives; to determine and approve the Chief Executive Officer's compensation level based upon the evaluation; to review and approve the compensation of officers and other key executives, incentive-compensation plans, equity-based plans and other compensation plans; to review and approve material changes to benefit programs, including new programs; to review the performance and development of Company management in achieving corporate goals and objectives; to assure that executive officers and other senior executives of the Company are compensated in a manner consistent with the strategy of the Company and competitive practice; to prepare a report on executive compensation as required by the Securities and Exchange Commission to be included in the annual proxy statement; and to oversee the Charitable Contributions Program. Each member of the Committee is an independent director, as defined in the applicable listing standards of the New York Stock Exchange. The Committee met five times in fiscal year 2004. Mr. Woods (Chairman), Mr. Solley and Mr. Trauscht are the members of the Committee. The Committee's charter is posted on the Company's website: www.escotechnologies.com and is available in print to any Stockholder who requests it.

The Nominating and Corporate Governance Committee's functions generally are to identify and recommend approval of individuals qualified to become Board members; to recommend director nominees for selection to the Board; to develop and recommend to the Board effective corporate governance guidelines; to oversee the Company's ethics programs; and to lead the Board in its annual review of the Board's performance. The Committee will consider candidates for election as directors recommended by Stockholders and evaluate such individuals in the same manner as other candidates proposed to the Committee. All candidates must meet the legal, regulatory and exchange requirements applicable to members of the Board of Directors. The Committee has not established other specific minimum qualifications that must be met by a candidate in order to be considered for nomination by the Committee but requires that candidates have varied business and professional backgrounds; be persons of the highest integrity; possess sound business judgment and possess such other skills and experience as will enable the Board to act in the long term interests of the Stockholders. Additionally, the Committee may establish and utilize such other specific membership criteria as the Committee deems appropriate from time to time in light of the Board's need of specific skills and experience. The Committee may identify new candidates for nomination based on recommendations from Company management, employees, non-management directors, third party search firms, Stockholders and other third parties. Consideration of a new candidate typically involves the Committee's review of information pertaining to such candidate and a series of internal discussions, and may proceed to interviews with the candidate. New candidates are evaluated based on the above described criteria in light of the specific needs of the Board and the Company at the time. Incumbent directors whose terms are set to expire are evaluated based on the above described criteria, as well as a review of their overall past performance on the Board of Directors. The Committee has the authority to engage third-party search firms to identify candidates, but did not do so in fiscal year 2004. Stockholders who wish to recommend director candidates for the next Annual Meeting of Stockholders should notify the Nominating and Corporate Governance Committee no later than August 29, 2005. Submissions are to be addressed to the Nominating and Corporate Governance Committee, c/o the Company's Corporate Secretary, Alyson S. Barclay, at ESCO Technologies Inc., 8888 Ladue Road, Suite 200, St. Louis, MO 63124-2056, which submissions will then be forwarded to the Committee. The Nominating and Corporate Governance Committee is not obligated to nominate any such individual for election. No such Stockholder candidates have been received by the Company for this Annual Meeting. Each member of the Committee is an independent director, as defined in the applicable listing standards of the New York Stock Exchange. The Committee met five times in fiscal year 2004. Mr. Trauscht (Chairman) and Mr. Solley are the members of the Committee. The Committee's charter is posted on the Company's website: www.escotechnologies.com and is available in print to any Stockholder who requests it.

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Report of the Audit and Finance Committee

The Audit and Finance Committee (the Committee) oversees and monitors the Company's financial reporting process on behalf of the Board of Directors. Management has the primary responsibility for the financial statements and the reporting process, including the Company's systems of internal control. In fulfilling its oversight responsibilities, the Committee reviewed and discussed the audited financial statements to be included in the Annual Report on Form 10-K for the year ended September 30, 2004 with management, including a discussion of the quality and the acceptability of the Company's financial reporting practices.

The Committee reviewed with the independent auditors, who are responsible for expressing an opinion on the conformity of those audited financial statements with accounting principles generally accepted in the United States of America, their judgments as to the quality and the acceptability of the Company's financial reporting and such other matters as are required to be discussed with the Committee under auditing standards generally accepted in the United States of America. In addition, the Committee discussed with the independent auditors the auditors' independence from management and the Company, including the impact of non-audit-related services provided to the Company and the matters in the auditors' written disclosures and the letter required by Standard No. 1 of the Independence Standards Board. The Committee also discussed with the independent auditors the matters required to be discussed by Statements on Auditing Standards No. 61.

The Committee also discussed with the Company's internal audit executive and independent auditors the overall scope and plans for their respective audits. The Committee meets periodically with the internal audit executive and independent auditors, with and without management present, to discuss the results of the examinations, their evaluations of the Company's internal controls, and the overall quality of the Company's financial reporting.

In reliance on the reviews and discussions referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Annual Report on Form 10-K for the fiscal year ended September 30, 2004 for filing with the Securities and Exchange Commission. The Committee also evaluated and reappointed the Company's independent auditors for fiscal 2005.

The Audit and Finance Committee

W.S. Antle III, Chairman

J.M. McConnell

J.M. Stolze

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Executive Compensation

Report Of The Human Resources And Compensation Committee

On Executive Compensation

Introduction

The following report is provided by the Human Resources and Compensation Committee of the Board of Directors (the Committee). The Committee supervises the Company's Executive Compensation Program (the Program) and is directly responsible for compensation actions affecting the executive officers and other senior officers of the Company. In this regard, the role of the Committee is to oversee ESCO's compensation plans and policies, annually review and approve all decisions relative to executive officers' compensation, and administer the plans (including the review and approval of equity awards to executive officers). The Committee's charter reflects these various responsibilities, and the Committee and the Board periodically review and revise the charter. The Committee's membership is determined by the Board and is composed entirely of independent directors. The Committee meets at scheduled times during the year, and it also considers and takes action by written consent. The Committee Chairman reports on Committee actions and recommendations at Board meetings. ESCO's Human Resources Department supports the Committee in its work and in some cases acts pursuant to delegated authority to fulfill various functions in administering ESCO's compensation programs. In addition, the Committee has the authority to engage the services of outside advisers, experts and others to assist the Committee. Last year, the Committee engaged a compensation consulting firm to assist the Committee in its review of the compensation for the executive officers.

Executive Compensation Philosophy

The Company's general compensation philosophy is that total cash compensation should vary with ESCO's performance in achieving financial and non-financial objectives, and that long-term compensation should be closely aligned with the Stockholders' interests.

The Program is designed and administered to relate executive compensation to four basic objectives:

Competitive Position: The Program is designed to pay competitive compensation so the Company can attract and retain highly qualified executives. To assist it in determining competitive compensation practices, the Committee utilizes information about compensation levels of peer companies and other industrial companies, including information provided by nationally-recognized, independent executive compensation consultants. When compensation varies from competitive levels, the Committee makes appropriate adjustments over time through the annual compensation planning process.

Company Performance: The Program is designed to reflect overall Company performance, with appropriate consideration of conditions that exist in the industries in which it engages. In determining compensation levels and compensation changes, the Committee considers the Company's overall performance in meeting both short-term and long-term objectives, achievement of operating objectives, performance in key areas such as Stockholder value, economic profit, growth and earnings per share, as well as progress toward long-term strategic objectives.

Stockholder Return: The Program has been designed to establish a direct link between the interests of the Company's executives and its Stockholders. This is accomplished by allocating a portion of senior management compensation to stock-based programs tied directly to Stockholder return and by establishing executive officer and other senior officer stock ownership guidelines.

Individual Performance: In addition to the above factors, the Committee considers the executive's individual performance and contributions to the Company's results in determining appropriate compensation levels.

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The Executive Compensation Program

To achieve the above objectives, the Program consists of three basic elements:

Base Salary: The base salary of each executive is reviewed annually and set by the Committee generally at the beginning of each fiscal year. Salary changes reflect overall Company performance, pay competitiveness and the individual's performance. The targeted percentage of total cash compensation represented by base salary varies based on the level of the position, with a target of approximately 60% for the Chairman and Chief Executive Officer (the CEO) and the President and Chief Operating Officer (the COO), and approximately 70% for the Vice President and Chief Financial Officer and the Vice President, Secretary and General Counsel.

Annual Cash Incentive Compensation: A substantial portion of each executive's annual cash compensation is tied to Company performance through the Company's Performance Compensation Plan (PCP), an annual cash incentive compensation program. The target percentage of total cash compensation represented by the PCP plan varies based on the level of the position, with a target of approximately 40% for the CEO and the COO and approximately 30% for the other executive officers. This at risk component closely links the executives' pay to the Company's financial results and provides for compensation variability through lower incentive payments in times of poor financial performance and higher compensation in times of strong performance. The Committee determines the annual PCP payment for each executive after the end of each fiscal year on the basis of a combination of objective targets and subjective evaluations of Company performance, considering market conditions and industry circumstances, in key areas such as earnings per share, shareholder value, economic profit, growth and other factors. The demonstrated individual performance of the executive as measured against strategic management objectives is also considered in the determination of the PCP payment. The types and relative importance of specific financial and other business objectives vary among the Company's executives depending upon their position and the particular function(s) for which they are responsible.

Long-Term Incentive Compensation: To align the interests of the Company's management directly with those of Stockholders, a portion of executive total compensation is provided by stock-based, long-term compensation plans. To place emphasis on Stockholder return, the Company has historically implemented stock option, performance share, performance-accelerated restricted stock (PARS) and restricted stock programs. In the past three years, only stock options and PARS have been awarded to the executive officers. These awards are included in the accompanying tables.

The Company's stock option programs provide for the award of incentive stock options, non-qualified stock options, and stock appreciation rights (SARs). No SARs have been awarded to date. All options granted to date, when first issued, have been awarded at an exercise price equal to the fair market value of the stock on the date of the award. Accordingly, the executive is rewarded only if the market price of the Company's stock appreciates. Since options vest over time, the Company periodically grants new options to provide continuing incentives for future performance. The size of previous grants and the number of options held are considered by the Committee, but are not entirely determinative of future grants. Like base pay, the grants are set with regard to competitive considerations, and each executive's actual grant is based upon individual performance and the executive's potential for future contributions.

The PARS program allows shares to be earned upon the achievement of specific stock price targets. Vesting is contingent on continued employment for a specified period after the shares are earned. However, awards not earned by stock performance will nevertheless vest and be distributed at the end of the employment period established for the award, provided the recipient continues in the employment of the Company.

Stock-based programs encourage Stockholder value creation, as this component of the compensation system is designed to retain senior executives and motivate them to improve the market value of the stock over a number of years.

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Stockholding Guidelines

Because the Committee believes in linking the interests of management and Stockholders, the Board has stockholding guidelines for the Company's executive officers. The guidelines specify a number of shares that each executive officer must accumulate and hold within five years of the effective date of the program or the date of appointment as, or promotion to, an officer. The specific share requirements are based on total cash compensation and are five times for the CEO, and three times for each of the other executive officers.

Fiscal Year 2004 Executive Officer Compensation

Fiscal year 2004 base salaries for the executive officers, which are shown in the Summary Compensation Table on page 12, were set at the beginning of fiscal year 2004. The salaries were set based on a subjective evaluation of fiscal year 2003 performance and salary levels compared to the Company's filtration/fluid flow comparison group and a group of broader industrial companies, consistent with the methodology described below.

In determining fiscal year 2004 target total cash compensation (base salary and PCP target percentages) for the executive officers, the Committee considered the competitiveness of cash compensation levels compared to the two comparison groups described above. The Committee utilized information from an executive compensation report prepared by a nationally-recognized, independent, compensation consulting firm. The report compared the Company's compensation practices to the two comparison groups by employee positions and levels consistent with the Company's executive officers. The report indicated that at the start of fiscal year 2004 total cash compensation of the CEO, including base salary and the annual incentive compensation, was below the 25th percentile for chief executive officers of the comparison companies, and target total cash compensation of the Company's other executive officers was below the median level for comparable senior officers of the comparison companies.

At the start of the fiscal year, the target total 2004 compensation of the CEO, including base salary, annual incentive cash compensation and long-term incentive compensation, was below the median for the comparison companies, and the target total compensation for the other executive officers was below the median total compensation for the comparable senior officers of the comparison companies.

In fiscal 2004, the Company recorded net sales of \$422.1 million, an increase of \$25.4 million, or 6.4%, over fiscal 2003 sales of \$396.7 million. Fiscal 2004 net earnings from continuing operations were \$37.8 million, or \$2.84 per share, compared with fiscal 2003 net earnings from continuing operations of \$26.7 million, or \$2.04 per share. Net earnings from continuing operations increased approximately 42% year over year. Net earnings/ (loss) were \$35.7 million, or \$2.68 per share, \$(41.1) million, or \$(3.13) per share, and \$21.8 million, or \$1.67 per share, in fiscal 2004, 2003 and 2002, respectively.

The 2004 results of operations included the impact of severance and move costs related to the closure of the Company's Puerto Rican manufacturing facility. The 2003 results of operations included the following items: the operating results from discontinued operations; the impact of the closure of the Puerto Rican manufacturing facility and the U.K. facility consolidations; the impact of the Management Transition Agreement (MTA) between the Company and its former Chairman; the impact of the interest rate swap charge related to the synthetic lease obligation; the net costs related to the settlement of the Whatman Manufacturing Supply Agreement (MSA); and the gain related to a favorable patent infringement settlement. The 2002 results of operations included the costs recognized in fiscal 2002 related to the MTA.

Taking into consideration the factors applicable to the annual cash incentive compensation component of executive compensation as described above, after the close of the fiscal year, the Committee approved a PCP payment for fiscal year 2004 of \$480,000 for the CEO. In determining this amount, the Committee considered the factors identified above, with 50% of the award based upon achievement of the EPS targets, 35% based upon the achievement of other factors, and 15% based on the execution of individual objectives which were established with the input of the Committee at the beginning of fiscal 2004.

The fiscal 2004 total cash compensation of the Company's other executive officers is detailed in the Summary Compensation Table on page 12.

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The Committee believes that stock ownership by key executives provides a valuable and important incentive for their continued best efforts and diligence, and provides for the continuing alignment of their interests with Stockholders. To facilitate these objectives, in fiscal 2004, the Committee granted the executive officers equity awards in the form of stock options and PARS. The Committee awarded the CEO 12,700 stock options and 6,000 shares of PARS. The specifics on the equity awards provided to the other executive officers are detailed in the Summary Compensation Table on page 12. The option price of all such stock options awarded was the fair market value on the date of award. The PARS awards established higher share price targets than previous awards, and further aligned the long term interests of the executive officers with those of Stockholders. These shares will be earned subject to the achievement of specified stock price target levels over the period from October 2005 through September 2008. However, awards not earned by stock performance will nevertheless vest and be distributed at the end of the service period established for the award. The individual equity grant amounts were based on internal factors such as the size of prior grants, relative job scope and contributions made during the past year, as well as a review of publicly available data on executive officer compensation provided by an independent nationally-recognized consulting firm.

Under the PARS program, the CEO earned and received a payout equivalent to 10,666 shares in fiscal 2004, and the other executive officers, as a group, earned and received a payout equivalent to 21,999 shares during fiscal 2004. Additionally, as a result of achievement in fiscal 2004 of the share price targets established for other awards, the CEO earned an additional 10,667 shares, which will vest upon his continued service through March 31, 2005, and the other executive officers, as a group, earned an additional 21,999 shares, which will vest upon their continued service through March 31, 2005.

The executive officers have employment agreements with the Company as described on page 15, and are also covered by a Severance Plan which is described on page 15.

Section 162(m) of the Internal Revenue Code denies a federal income tax deduction for compensation in excess of \$1 million paid to any of the Company's highest paid executive officers unless the compensation qualifies for a performance-based exception. The 1999 Stock Option Plan was generally designed to permit awards that satisfy the performance-based exception of Section 162(m). The 2001 Stock Incentive Plan and the 2004 Incentive Compensation Plan also were generally designed to permit awards that satisfy that exception; however, these Plans also permit awards that may not satisfy such exception. The Company does not expect compensation levels of its executive officers to exceed the Section 162(m) limit in the foreseeable future.

Summary

The Committee believes the Company's compensation program has been designed and managed by the Committee to directly link the compensation of the Company's executives to Company performance, individual performance and Stockholder return. The total direct compensation earned in fiscal 2004 by the CEO and the other executive officers is below market median as determined by survey data from similar companies in the filtration/fluid flow comparison group and the broader industrial companies, is commensurate with their executive officer tenure, and is appropriate relative to the Company's fiscal 2004 performance. The Committee will continue to address these compensation levels over time, consistent with Company and individual performance, and will continue to emphasize performance and stock-based compensation that links management and Stockholder interests.

The Human Resources and
Compensation Committee

J.D. Woods, Chairman
L.W. Solley
D.C. Trauscht

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The following table contains certain information concerning compensation for each of the last three fiscal years for all services rendered in all capacities to the Company and its subsidiaries of the Chairman and Chief Executive Officer and the other three executive officers serving at September 30, 2004. No information for Mr. Muenster is provided for fiscal year 2002 because he first became an executive officer in fiscal year 2003.

Name and Principal Position	Fiscal Year	Annual Compensation			Long-Term-Compensation			
		(\$) Salary	(\$) Bonus	(\$) Other Annual Compensation	Awards		Payouts	
					(\$) Restricted Stock Awards(1)	(#) Securities Underlying Options	(\$) LTIP Payouts	(\$) All Other Compen- sation(2)
V.L. Richey, Jr. Chairman and Chief Executive Officer	2004 2003 2002	360,000 280,000 171,250	480,000 120,000 125,000	7,081 55,873 81,722(4)	295,200(3) 0 574,038(5)	12,700 0 44,000	0 0 0	17,375 6,069 2,809
C.J. Kretschmer President and Chief Operating Officer	2004 2003 2002	260,000 210,000 167,500	330,000 98,000 110,000	5,876 11,324 44,066(6)	233,700(3) 0 426,277(7)	5,100 0 33,500	0 0 0	10,818 960 841
G.E. Muenster Vice President and Chief Financial Officer	2004 2003	195,000 155,000	170,000 49,000	3,298 27,953(8)	118,080(3) 0	3,400 0	0 0	2,203 1,162
A.S. Barclay Vice President, Secretary and General Counsel	2004 2003 2002	155,000 141,000 131,750	140,000 42,000 70,110	4,381 34,360(9) 32,533(10)	88,560(3) 0 232,078(11)	2,800 0 14,500	0 0 0	8,318 2,115 3,265

- (1) Restricted shares shown in this column are performance-accelerated restricted shares that will vest if the named officer continues in the employment of the Company through the employment service period established for the award; however, these shares will vest earlier upon achievement of specified stock price targets established for the award and continued employment of the named officer through March 31 of the year following the end of the fiscal year in which the target is achieved. Each target level is based on the average stock price over a period of thirty consecutive trading days. All awards provide for acceleration of vesting in the event of a change in control of the Company. Dividends, if any, will not be paid prior to the vesting and distribution of the shares.
- (2) Amounts shown in this column are Company cash match contributions under the Employee Stock Purchase Plan and/or the Employee Savings Investment Plan whereby the Company matches certain percentages of the employees' contributions. See Retirement Plan on page 14.
- (3) Represents fair market value of \$49.20 per share at the time of award for the shares awarded as follows: Mr. Richey 6,000 shares; Mr. Kretschmer 4,750 shares; Mr. Muenster 2,400 shares; Ms. Barclay 1,800 shares. Those shares will vest regardless of stock price target achievement if the named officer continues in the employment of the Company through the vesting date, September 30, 2008. At September 30, 2004, each of these individuals held an aggregate of unvested Company restricted stock having a value as follows: Mr. Richey 35,134 shares/ \$2,380,680; Mr. Kretschmer 28,417 shares/ \$1,925,536; Mr. Muenster 17,600 shares/ \$1,192,576; Ms. Barclay 17,433 shares/ \$1,181,260.
- (4) Includes \$44,851 for club expenses.
- (5) Represents fair market value of \$25.34 per share at the time of award for 8,000 shares awarded and of \$34.81 per share at the time of award for 10,667 shares awarded. On April 1, 2003, a payout equivalent to 2,667 of these shares was made. On March 31, 2004, a payout equivalent to 2,666 of these shares was made. On March 31, 2005 and on March 31, 2006, 2,667 shares and 10,667 shares, respectively, will vest if Mr. Richey continues in the employment of the Company.
- (6)

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Includes reimbursement of \$8,520 for car expenses and \$8,723 for interest costs on personal loans for the purchase of Common Shares under the Executive Stock Purchase Plan. These loans have been liquidated by Mr. Kretschmer.

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- (7) Represents fair market value of \$25.34 per share at the time of award for 4,000 shares awarded and of \$34.81 per share at the time of award for 9,334 shares awarded. On April 1, 2003, a payout equivalent to 1,334 of these shares was made. On March 31, 2004, a payout equivalent to 1,333 of these shares was made. On March 31, 2005 and on March 31, 2006, 1,333 shares and 9,334 shares, respectively, will vest if Mr. Kretschmer continues in the employment of the Company.
- (8) Includes reimbursement of \$15,056 for car expenses.
- (9) Includes reimbursement of \$14,938 for car expenses and \$7,242 for club expenses.
- (10) Includes reimbursement of \$6,043 for car expenses, \$5,966 for club expenses, and \$8,723 for interest costs on personal loans for the purchase of Common Shares under the Executive Stock Purchase Plan. These loans have been liquidated by Ms. Barclay.
- (11) Represents fair market value of \$34.81 per share at the time of award for 6,667 shares awarded. On March 31, 2006, these shares will vest if Ms. Barclay continues in the employment of the Company.

The Company's stock option and performance-accelerated restricted stock award agreements applicable to the named executive officers generally provide for acceleration of vesting and, in certain cases, payout of awards in the event of a change in control of the Company, as defined in such agreements.

OPTION GRANTS IN LAST**FISCAL YEAR****Individual Grants**

Name	(#) of Securities Underlying Options Granted(1)	% of Total Options Granted to Employees In Fiscal Year	(\$ Share) Exercise Price	Expiration Date	(\$) Grant Date Present Value(2)
V.L. Richey, Jr.	12,700	8.71	\$49.505	5/5/2009	\$160,367
C.J. Kretschmer	5,100	3.50	49.505	5/5/2009	64,399
G.E. Muenster	3,400	2.33	49.505	5/5/2009	42,933
A.S. Barclay	2,800	1.92	49.505	5/5/2009	35,356

- (1) These stock option grants are non-transferable, have a term of five years from the date of grant, and have an exercise price equal to 100% of the fair market value on the date of grant. The options are exercisable as follows: one-third of the options granted may be exercised on or after one year after the date of grant, an additional one-third on or after two years after the date of grant, and the final one-third on or after three years after the date of grant. In the event of a change in control of the Company, 100% of the options granted immediately vest.
- (2) Estimated present values based on the Black-Scholes option pricing model, a mathematical formula used to value options traded on stock exchanges. The following assumptions were used in applying the model to calculate the values: expected future stock price volatility rate of 16.44%; risk-free rate of return of 4.593% for the option term; annual dividend yield of 0%; and a five-year option term. No adjustments have been made for non-transferability or risk of forfeiture. The actual value of the options will depend on the market price of the shares on the date options are exercised, and may vary significantly from the theoretical values estimated by the Black-Scholes model.

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**AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR
AND FISCAL YEAR-END OPTION VALUES**

The following table provides certain information concerning stock option exercises during fiscal year 2004 by each of the named executive officers and the value of their unexercised options at September 30, 2004.

(#)

(\$)