

EZ EM INC  
Form 10-Q  
April 13, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 4, 2006

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-11479

E-Z-EM, Inc.

(Exact name of registrant as specified in its charter)

Delaware

11-1999504

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(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification No.)

**1111 Marcus Avenue, Lake Success, New York**

(Address of principal executive offices)

**11042**

(Zip Code)

**(516) 333-8230**

Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of April 7, 2006, there were 10,857,140 shares of the issuer's common stock outstanding.

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**E-Z-EM, Inc. and Subsidiaries**

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E-Z-EM, Inc. and Subsidiaries

**CONSOLIDATED BALANCE SHEETS**

(in thousands)

ASSETS	March 4, 2006	May 28, 2005
	(unaudited)	(audited)
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 4,880	\$ 10,183
Debt and equity securities, at fair value	26,807	18,419
Accounts receivable, principally trade, net	22,538	17,677
Inventories, net	27,462	22,822
Refundable income taxes	2,363	1,444
Other current assets	5,581	4,705
	<u>89,631</u>	<u>75,250</u>
<b>PROPERTY, PLANT AND EQUIPMENT - AT COST,</b>		
less accumulated depreciation and amortization	12,972	13,256
<b>INTANGIBLE ASSETS, less accumulated</b>		
amortization	4,309	4,867
<b>DEBT AND EQUITY SECURITIES, at fair value</b>		
	1,381	746
<b>OTHER ASSETS</b>		
	10,192	7,936
<b>NONCURRENT ASSETS HELD FOR DISPOSAL</b>		
		3,593
	<u>118,485</u>	<u>105,648</u>
Total assets	\$ 118,485	\$ 105,648

The accompanying notes are an integral part of these statements.

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E-Z-EM, Inc. and Subsidiaries

### CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

LIABILITIES AND STOCKHOLDERS EQUITY	March 4, 2006	May 28, 2005
	(unaudited)	(audited)
<b>CURRENT LIABILITIES</b>		
Notes payable	\$ 170	\$ 347
Current maturities of long-term debt	80	99
Accounts payable	4,541	5,069
Accrued liabilities	10,611	9,916
Accrued income taxes	143	207
	<u>          </u>	<u>          </u>
Total current liabilities	15,545	15,638
LONG-TERM DEBT, less current maturities	23	85
OTHER NONCURRENT LIABILITIES	4,136	4,205
	<u>          </u>	<u>          </u>
Total liabilities	19,704	19,928
	<u>          </u>	<u>          </u>

### COMMITMENTS AND CONTINGENCIES

### STOCKHOLDERS EQUITY

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LIABILITIES AND STOCKHOLDERS EQUITY	March 4, 2006	May 28, 2005
Preferred stock, par value \$.10 per share - authorized, 1,000,000 shares; issued, none		
Common stock, par value \$.10 per share - authorized, 16,000,000 shares; issued and outstanding 10,857,140 shares at March 4, 2006 and 10,827,772 shares at May 28, 2005 (excluding 89,205 shares held in treasury at March 4, 2006 and May 28, 2005)	1,086	1,083
Additional paid-in capital	29,642	28,478
Retained earnings	62,917	54,497
Accumulated other comprehensive income	5,136	1,662
	<u>          </u>	<u>          </u>
Total stockholders equity	98,781	85,720
	<u>          </u>	<u>          </u>
Total liabilities and stockholders equity	\$ 118,485	\$ 105,648
	<u>          </u>	<u>          </u>

The accompanying notes are an integral part of these statements.

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E-Z-EM, Inc. and Subsidiaries

**CONSOLIDATED STATEMENTS OF EARNINGS**

(unaudited)

(in thousands, except per share data)

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	Thirteen weeks ended		Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	March 4, 2006	February 26, 2005		
Net sales	\$ 32,265	\$ 30,833	\$ 101,253	\$ 81,067
Cost of goods sold	19,487	18,106	57,274	46,462
<b>Gross profit</b>	<b>12,778</b>	<b>12,727</b>	<b>43,979</b>	<b>34,605</b>
Operating expenses				
Selling and administrative	10,094	8,923	31,909	26,192
Plant closings and operational restructuring costs	218	649	353	2,074
Gain on sale of real property	(1,205)		(1,205)	
Research and development	1,563	1,421	4,318	3,919
<b>Total operating expenses</b>	<b>10,670</b>	<b>10,993</b>	<b>35,375</b>	<b>32,185</b>
<b>Operating profit</b>	<b>2,108</b>	<b>1,734</b>	<b>8,604</b>	<b>2,420</b>
Other income (expense)				
Interest income	230	83	543	230
Interest expense	(102)	(84)	(343)	(249)
Other, net	148	1,496	(178)	2,522
<b>Earnings from continuing operations before income taxes</b>	<b>2,384</b>	<b>3,229</b>	<b>8,626</b>	<b>4,923</b>
Income tax provision (benefit)	(1,958)	311	206	551
<b>Earnings from continuing operations</b>	<b>4,342</b>	<b>2,918</b>	<b>8,420</b>	<b>4,372</b>
Earnings from discontinued operation, net of income tax provision				1,228
<b>NET EARNINGS</b>	<b>\$ 4,342</b>	<b>\$ 2,918</b>	<b>\$ 8,420</b>	<b>\$ 5,600</b>
Basic earnings per common share				
From continuing operations	\$ 0.40	\$ 0.27	\$ 0.78	\$ 0.41
From discontinued operation, net of income tax provision				0.11

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	Thirteen weeks ended		Forty weeks ended	Thirty-nine weeks ended
			March 4, 2006	February 26, 2005
	\$ 0.40	\$ 0.27	0.78	0.52
Net earnings			\$	\$
Diluted earnings per common share				
From continuing operations	\$ 0.39	\$ 0.27	\$ 0.76	\$ 0.40
From discontinued operation, net of income tax provision				0.11
Net earnings	\$ 0.39	\$ 0.27	\$ 0.76	\$ 0.51
Weighted average common shares				
Basic	10,855	10,772	10,846	10,751
Diluted	11,190	10,960	11,100	10,943

The accompanying notes are an integral part of these statements.

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E-Z-EM, Inc. and Subsidiaries

**CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME**

Forty weeks ended March 4, 2006

(unaudited)

(in thousands, except share data)



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	Common stock		Additional paid-in capital	Retained earnings	Accumulated other comprehensive income	Total	Compre- hensive income
	Shares	Amount					
Balance at May 28, 2005	10,827,772	\$ 1,083	\$ 28,478	\$ 54,497	\$ 1,662	\$ 85,720	
Exercise of stock options	21,368	2	132			134	
Income tax benefits on stock options exercised			863			863	
Compensation related to stock option plans, net of income tax benefit			41			41	
Issuance of stock	8,000	1	128			129	
Net earnings				8,420		8,420	\$ 8,420
Unrealized holding gain on debt and equity securities					400	400	400
Foreign currency translation adjustments					3,074	3,074	3,074
<b>Comprehensive income</b>							<b>\$ 11,894</b>
Balance at March 4, 2006	10,857,140	\$ 1,086	\$ 29,642	\$ 62,917	\$ 5,136	\$ 98,781	

The accompanying notes are an integral part of this statement.

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E-Z-EM, Inc. and Subsidiaries

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(unaudited)

(in thousands)

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	Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	<u>                    </u>	<u>                    </u>
Cash flows from operating activities:		
Net earnings	\$ 8,420	\$ 5,600
Earnings from discontinued operation, net of tax		(1,228)
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities		
Depreciation and amortization	2,732	2,262
Impairment of long-lived assets	257	
Gain on sale of assets	(1,164)	
Gain on sale of investments		(2,385)
Provision for doubtful accounts	45	69
Tax benefit on exercise of stock options	863	1,217
Deferred income tax provision (benefit)	(1,288)	81
Stock option compensation cost	65	406
Other non-cash items	126	98
Changes in operating assets and liabilities		
Accounts receivable	(4,906)	(4,623)
Inventories	(4,640)	(3,440)
Other current assets	(1,822)	(913)
Other assets	112	(473)
Accounts payable	(528)	2,397
Accrued liabilities	(95)	778
Accrued income taxes	(64)	31
Other noncurrent liabilities	54	184
Net cash provided by operating activities of discontinued operation		567
	<u>                    </u>	<u>                    </u>
Net cash provided by (used in) operating activities	(1,833)	628
	<u>                    </u>	<u>                    </u>
Cash flows from investing activities:		
Additions to property, plant and equipment, net	(1,314)	(2,997)
Proceeds from sale of assets	4,774	
Advanced royalty fee	(650)	
Purchase of intangible assets		(555)
Proceeds from sale of investment at cost		575
Investment at cost		(90)
Available-for-sale securities		
Purchases	(142,085)	(23,545)
Proceeds from sale	133,697	23,108
Net cash used in investing activities of discontinued operation		(11,140)
	<u>                    </u>	<u>                    </u>
Net cash used in investing activities	(5,578)	(14,644)
	<u>                    </u>	<u>                    </u>

The accompanying notes are an integral part of these statements.

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E-Z-EM, Inc. and Subsidiaries

**CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)**

(unaudited)

(in thousands)

	<b>Forty weeks ended March 4, 2006</b>	<b>Thirty-nine weeks ended February 26, 2005</b>
	<u>          </u>	<u>          </u>
Cash flows from financing activities:		
Repayments of debt	\$ (230)	\$ (263)
Proceeds from issuance of debt		93
Proceeds from repayment of debt by discontinued operation		3,000
Dividends paid		(3,220)
Proceeds from exercise of stock options	134	225
Proceeds from issuance of stock in connection with the stock purchase plan	3	10
Cash distributed with discontinued operation		(8,453)
Net cash provided by financing activities of discontinued operation		18,958
	<u>          </u>	<u>          </u>
Net cash provided by (used in) financing activities	(93)	10,350
	<u>          </u>	<u>          </u>
Effect of exchange rate changes on cash and cash equivalents	2,201	1,744
	<u>          </u>	<u>          </u>

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	Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	<u>          </u>	<u>          </u>
DECREASE IN CASH AND CASH EQUIVALENTS	(5,303)	(1,922)
<b>Cash and cash equivalents</b>		
Beginning of period	<u>10,183</u>	<u>12,334</u>
End of period	<u>\$ 4,880</u>	<u>\$ 10,412</u>
<b>Supplemental disclosures of cash flow information:</b>		
<b>Cash paid during the period for:</b>		
Interest	<u>\$ 280</u>	<u>\$ 83</u>
Income taxes (net of \$2 in refunds in 2006)	<u>\$ 1,721</u>	<u>\$ 2,013</u>

The accompanying notes are an integral part of these statements.

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE A NATURE OF BUSINESS AND BASIS OF PRESENTATION**

**Nature of Business**

E-Z-EM, Inc. and its subsidiaries ( the Company or E-Z-EM ) is a leading provider of medical products used by radiologists, gastroenterologists and speech language pathologists primarily in screening for and diagnosing diseases and disorders of the gastrointestinal (GI) tract. Products are used for colorectal cancer screening, evaluation of swallowing disorders (dysphagia), and testing for other diseases and disorders of the GI system. The Company is also a third-party contract manufacturer, a business that enables the Company to leverage its capacity in quality control, process, automation and manufacturing. Prior to the spin-off of AngioDynamics, Inc. ( AngioDynamics ) on October 30, 2004, the Company was also a provider of innovative medical devices used in minimally invasive, image-guided procedures to treat peripheral vascular disease, or PVD. AngioDynamics designed, developed, manufactured and marketed a broad line of therapeutic and diagnostic devices that enabled interventional physicians (interventional radiologists, vascular surgeons and others) to treat PVD and other non-coronary diseases.

**Basis of Presentation**

The consolidated balance sheet as of March 4, 2006, the consolidated statement of stockholders' equity and comprehensive income for the forty weeks ended March 4, 2006, and the consolidated statements of earnings and cash flows for the periods ended March 4, 2006 and February 26, 2005, have been prepared by the Company without audit. The consolidated balance sheet as of May 28, 2005 was derived from audited consolidated financial statements. In the opinion of management, all adjustments (which include normal recurring adjustments) necessary to present fairly the financial position, changes in stockholders' equity and comprehensive income, results of operations and cash flows at March 4, 2006 (and for all periods presented) have been made.

Certain information and footnote disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. It is suggested that these consolidated financial statements be read in conjunction with the financial statements and notes thereto included in the Annual Report on Form 10-K for the fiscal year ended May 28, 2005 filed by the Company on August 11, 2005. The results of operations for the periods ended March 4, 2006 and February 26, 2005 are not necessarily indicative of the operating results for the respective full years.

E-Z-EM, Inc. and Subsidiaries

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 4, 2006 and February 26, 2005

(unaudited)

### NOTE A NATURE OF BUSINESS AND BASIS OF PRESENTATION (continued)

The consolidated financial statements include the accounts of E-Z-EM, Inc. and all wholly owned subsidiaries, as well as the accounts of AngioDynamics, an 80.4%-owned subsidiary, through its spin-off on October 30, 2004. As a result of the spin-off, AngioDynamics is reported separately as a discontinued operation for the thirty-nine weeks ended February 26, 2005 within the consolidated financial statements (see Note B - Discontinued Operation). All significant intercompany balances and transactions have been eliminated.

### NOTE B DISCONTINUED OPERATION

On May 27, 2004, AngioDynamics, the Company's former subsidiary, sold 1,950,000 shares of its common stock at \$11.00 per share through an initial public offering (IPO). Proceeds from the IPO, net of certain financing costs, totaling \$19,949,000 were received by AngioDynamics on June 2, 2004. At May 29, 2004, E-Z-EM owned 9,200,000 shares, or 82.5% of the 11,150,000 shares outstanding. On June 15, 2004, the underwriters of the IPO exercised their over-allotment option and acquired 292,500 shares at \$11.00 per share, less underwriting discounts and commissions, and on June 18, 2004, AngioDynamics received net proceeds of \$2,992,000. At June 15, 2004, E-Z-EM's ownership interest in AngioDynamics decreased to 80.4%.

On October 30, 2004, the Company completed the spin-off of AngioDynamics by means of a tax-free distribution of the Company's remaining 80.4% ownership of AngioDynamics. In February 2004, the Company received a favorable private letter ruling from the Internal Revenue Service regarding the tax-free treatment of the distribution of E-Z-EM's remaining ownership in AngioDynamics. The Company made a pro rata distribution of its 9,200,000 shares of AngioDynamics common stock on October 30, 2004 to E-Z-EM shareholders of record as of October 11, 2004 (the Record Date). Based on the shares outstanding of each company on the Record Date, E-Z-EM shareholders received .856377 of a share of AngioDynamics stock for each share of E-Z-EM stock they owned on the Record Date. For all periods presented, AngioDynamics is accounted for as a discontinued operation in the Company's financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for Impairment and Disposal of Long-Lived Assets. Amounts in the financial statements and related notes for all periods shown have been reclassified to reflect the discontinued operation.

In fiscal 2004, E-Z-EM entered into three agreements with AngioDynamics—a master separation and distribution agreement, a corporate agreement and a tax allocation and indemnification agreement—that relate to its relationship with AngioDynamics both before and after the separation of AngioDynamics from the Company. All of the agreements between the Company and AngioDynamics were made in the context of a parent-subsiary relationship and were negotiated in the overall context of the spin-off.

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE B DISCONTINUED OPERATION (continued)**

Summarized results of operations for AngioDynamics, including minority interest, as reported in earnings from discontinued operation in the accompanying consolidated statements of earnings are as follows:

	<b>Thirty-nine weeks ended February 26, 2005</b>
	<b>(in thousands)</b>
Net sales	
From unaffiliated customers	\$ 22,342
From affiliates	420
Total net sales	<u>\$ 22,762</u>
Earnings before income taxes and minority interest	\$ 2,628
Income tax provision	<u>1,103</u>
Earnings before minority interest	1,525
Minority interest	297

	<b>Thirty-nine weeks ended February 26, 2005</b>
	<u>                    </u>
	<u>                    </u>
Earnings from discontinued operation	\$ 1,228
	<u>                    </u>

For the thirty-nine weeks ended February 26, 2005, the results of operations for AngioDynamics represented twenty-two weeks activity.

**NOTE C - STOCK-BASED COMPENSATION**

At March 4, 2006, the Company had three stock-based compensation plans. The Company accounts for these plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees and related interpretations. Accordingly, no compensation expense has been recognized under these plans concerning options granted to key employees and to members of the Board of Directors, as all such options granted had an exercise price equal to or greater than the market value of the underlying common stock on the date of grant. For the thirteen weeks ended March 4, 2006 and February 26, 2005, compensation expense of \$21,000 was recognized under these plans for options granted to a former director serving as a consultant. For the forty weeks ended March 4, 2006 and the thirty-nine weeks ended February 26, 2005, compensation expense of \$65,000 and \$406,000, respectively, was recognized under these plans for options granted to a former director serving as a consultant.

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)



**NOTE C - STOCK-BASED COMPENSATION (continued)**

The following table illustrates the effect on net earnings and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to options granted under these plans to key employees and to members of the Board of Directors:

	Thirteen weeks ended		Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	March 4, 2006	February 26, 2005		
	(in thousands, except per share data)			
Net earnings, as reported	\$ 4,342	\$ 2,918	\$ 8,420	\$ 5,600
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of income tax effects	(267)	(2,124)	(825)	(2,704)
Pro forma net earnings	\$ 4,075	\$ 794	\$ 7,595	\$ 2,896
Earnings per common share				
Basic - as reported	\$ .40	\$ .27	\$ .78	\$ .52
Basic - pro forma	.38	.07	.70	.27
Diluted - as reported	\$ .39	\$ .27	\$ .76	\$ .51
Diluted - pro forma	.36	.07	.68	.26

During the forty weeks ended March 4, 2006, options for 207,500 shares were granted at \$14.48 per share, options for 21,368 shares were exercised at prices ranging from \$3.55 to \$14.23 per share, options for 995 shares expired at \$3.55 per share, and options for 5,000 shares were forfeited at \$14.23 per share under the 1983, 1984 and 2004 Stock Option Plans.

E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE D - EARNINGS PER COMMON SHARE**

Basic earnings per share are based on the weighted average number of common shares outstanding without consideration of potential common stock. Diluted earnings per share are based on the weighted average number of common and potential common shares outstanding. The calculation takes into account the shares that may be issued upon exercise of stock options, reduced by the shares that may be repurchased with the funds received from the exercise, based on the average price during the period.

The following table sets forth the reconciliation of the weighted average number of common shares:

	<b>Thirteen weeks ended</b>		<b>Forty</b>	<b>Thirty-nine</b>
	<b>March 4,</b>	<b>February 26,</b>	<b>weeks ended</b>	<b>weeks ended</b>
	<b>2006</b>	<b>2005</b>	<b>March 4,</b>	<b>February 26,</b>
			<b>2006</b>	<b>2005</b>
	(in thousands)			
Basic	10,855	10,772	10,846	10,751
Effect of dilutive securities (stock options)	335	188	254	192
Diluted	11,190	10,960	11,100	10,943

Excluded from the calculation of earnings per common share, are options to purchase 396,000 and 24,000 shares of common stock for the thirteen and thirty-nine weeks ended February 26, 2005, respectively, as their inclusion would be anti-dilutive. The range of exercise prices on the excluded options was \$13.45 to \$14.51 per share for the thirteen weeks ended February 26, 2005 and the exercise price on the excluded options was \$13.45 for the thirty-nine weeks ended February 26, 2005.

**NOTE E - EFFECTS OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In March 2004, the Financial Accounting Standards Board ( FASB ) Emerging Issues Task Force ( EITF ) released Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. EITF 03-1 provides guidance for determining whether impairment for certain debt and equity investments is other-than-temporary and the measurement of an impaired loss. Certain disclosure requirements of EITF 03-1 were adopted in fiscal 2004 and the Company has complied with the new disclosure requirements in its consolidated financial statements. The recognition and measurement requirements of EITF 03-1 were initially effective for reporting periods beginning after June 15, 2004. In September 2004, the FASB Staff issued FASB Staff Position ( FSP ) EITF 03-1-1 that delayed the effective date for certain measurement and recognition guidance contained in EITF 03-1. The FSP requires that entities continue to apply previously existing other-than-temporary guidance until a final consensus is reached. The Company does not anticipate that the issuance of a final consensus will materially impact its financial condition or results of operations.

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE E - EFFECTS OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS (continued)**

In November 2004, the FASB issued Statement of Financial Accounting Standards ( SFAS ) No. 151, Inventory Costs , an amendment of ARB No. 43, Chapter 4. The amendments made by SFAS No. 151 will improve financial reporting by clarifying that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and by requiring the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 24, 2004. The adoption of this statement is not expected to have a material impact on the Company's financial condition or results of operations.

In December 2004, the FASB issued SFAS No. 123 (R), Share-Based Payment , which revises SFAS No. 123, Accounting for Stock-Based Compensation and supercedes APB Opinion No. 25, Accounting for Stock Issued to Employees . SFAS No. 123 (R) establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. This statement focuses primarily on

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accounting for transactions in which an entity obtains employee services in share-based payment transactions. SFAS No. 123 (R) requires that the fair value of such equity instruments be recognized as an expense in the historical financial statements as services are performed. Prior to SFAS No. 123 (R), only certain pro forma disclosures of fair value were required. In April 2005, the Securities and Exchange Commission adopted a new rule that amended the compliance dates of SFAS No. 123 (R) to require the implementation no later than the beginning of the first annual reporting period beginning after June 15, 2005. The adoption of this statement may have a material impact on the Company's financial condition and results of operations commencing with the fiscal quarter ending September 2, 2006.

On December 31, 2004, the FASB issued FASB Staff Position No. FAS 109-2, Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004, ( FSP No. 109-2 ). This staff position provides accounting guidance on how companies should account for the effects of the American Jobs Creation Act of 2004 ( AJCA ) that was signed into law on October 22, 2004. FSP No. 109-2 gives a company additional time to evaluate the effects of the legislation on any plan for reinvestment or repatriation of foreign earnings for purposes of applying FASB Statement No. 109. The Company is investigating the repatriation provision to determine whether it might repatriate extraordinary dividends, as defined in the AJCA. The Company is currently evaluating all available U.S. Treasury guidance.

In June 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements. SFAS No. 154 changes the requirements for the accounting for

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E-Z-EM, Inc. and Subsidiaries

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 4, 2006 and February 26, 2005

(unaudited)

#### NOTE E - EFFECTS OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS (continued)

and reporting of a change in accounting principle. Previously, most voluntary changes in accounting principles required recognition via a cumulative effect adjustment within net income for the period of the change. SFAS No. 154 requires retrospective application to prior periods financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. SFAS No.

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154 is effective for accounting changes made in fiscal years beginning after December 15, 2005; however, SFAS No. 154 does not change the transition provisions of any existing accounting pronouncements. The Company does not believe the adoption of SFAS No. 154 will have a material impact on its financial condition or results of operations.

### NOTE F - COMPREHENSIVE INCOME

The components of comprehensive income, net of related tax, are as follows:

	Thirteen weeks ended		Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	March 4, 2006	February 26, 2005		
	(in thousands)			
Net earnings	\$ 4,342	\$ 2,918	\$ 8,420	\$ 5,600
Unrealized holding gain (loss) on debt and equity securities:				
Arising during the period	142	(43)	400	1,108
Reclassification adjustment for gains included in net earnings		(979)		(2,385)
Decrease in fair value on interest rate swap arising during the period				(55)
Foreign currency translation adjustments arising during the period	821	(1,538)	3,074	2,615
	821	(1,538)	3,074	2,615
Comprehensive income	\$ 5,305	\$ 358	\$ 11,894	\$ 6,883

The components of accumulated other comprehensive income, net of related tax, are as follows:

	March 4, 2006	May 28, 2005
	(in thousands)	
Unrealized holding gain on debt and equity securities	\$ 708	\$ 308
Cumulative translation adjustments	4,428	1,354
Accumulated other comprehensive income	\$ 5,136	\$ 1,662

March 4, 2006	May 28, 2005
_____	_____
_____	_____

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE G PLANT CLOSINGS AND OPERATIONAL RESTRUCTURING**

In February 2006, the Company's Executive Committee of the Board of Directors approved a plan to wind down and close the operations of Toho Kagaku Kenkyusho Co., Ltd. (Toho), a wholly owned Japanese subsidiary. The decision to close Toho resulted from an inability to generate income from operations and to grow the business due to a limited product offering and scope of operations. Also, a recent change in manufacturing location required a re-registration of Toho's principal products with Japanese regulatory authorities, resulting in a projected interruption of supply during the first quarter of fiscal 2007. Management plans a market withdrawal on a staged basis so that current inventory can be sold, accounts receivable collected and the property sold in an organized fashion, while also satisfying all outstanding liabilities. As a result of this plan, foreign currency translation losses of \$257,000 included in accumulated other comprehensive income have been charged to results of operations for the thirteen weeks ended March 4, 2006 in accordance with EITF Issue No. 01-5, Application of FASB Statement No. 52 to an Investment Being Evaluated for Impairment That Will Be Disposed Of. EITF 01-5 requires that accumulated foreign currency translation adjustments be included as part of the carrying amount of a foreign investment being evaluated for impairment under a committed plan of disposal. The Company expects to incur up to an additional \$400,000 in project costs, primarily severance related, over its next two fiscal quarters. The decision to close the Toho operations resulted in a deduction for U.S. Federal income tax purposes approximating \$6,904,000. During the thirteen weeks ended March 4, 2006, the Company recorded a Federal tax benefit of \$2,347,000 relating to this tax deduction.

In the fourth quarter of fiscal 2005, the Company substantially completed its plan to further streamline its operations, specifically by moving its powder-based barium production in Westbury, N.Y. to its manufacturing facility in Montreal, Canada. For the forty weeks ended March 4, 2006

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and the thirty-nine weeks ended February 26, 2005, project costs aggregated \$96,000 and \$2,074,000, respectively. At March 4, 2006 and May 28, 2005, the liability for this restructuring, which is included in accrued liabilities, approximated \$0 and \$598,000, respectively. On January 31, 2006, the Company completed the sale of its Westbury manufacturing facility for \$5,100,000. As a result, the Company recognized a gain on the sale of this property of \$1,205,000 during the thirteen weeks ended March 4, 2006.

	Remaining at May 28, 2005	Recorded	Paid	Remaining at March 4, 2006
	(in thousands)			
Project costs	\$ 598	\$ 96	\$ (694)	\$ 0

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E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE H - INVENTORIES**

Inventories consist of the following:

<b>March 4, 2006</b>	<b>May 28, 2005</b>
--------------------------	-------------------------

	_____	_____
	(in thousands)	
Finished goods	\$ 12,987	\$ 10,305
Work in process	243	573
Raw materials	14,232	11,944
	_____	_____
	\$ 27,462	\$ 22,822
	_____	_____

**NOTE I DEBT AND EQUITY SECURITIES**

During the thirteen and thirty-nine weeks ended February 26, 2005, the Company sold 100,000 shares and 300,000 shares, respectively, of its investment in Cedara Software Corporation. The Company recognized gains on these sales totaling \$979,000 and \$2,385,000, respectively, during the thirteen and thirty-nine weeks ended February 26, 2005, which are included in the consolidated statements of earnings under the caption Other, net .

**NOTE J INCOME TAXES**

For the thirteen weeks ended March 4, 2006, the Company reported an income tax benefit of \$1,958,000 against earnings from continuing operations before income taxes of \$2,384,000 due primarily to: i) a tax benefit of \$2,347,000 associated with the closing of the Company's Japanese subsidiary; and ii) the reversal of a valuation allowance of \$496,000 relating to a previously impaired, non-core equity security, since it is now more likely than not that such benefit will be realized. For the forty weeks ended March 4, 2006, the Company's unusually low effective tax rate of 2% differed from the Federal statutory tax rate of 34% due primarily to: i) a tax benefit of \$2,347,000 associated with the closing of the Company's Japanese subsidiary; and ii) the reversal of a valuation allowance of \$496,000 relating to a previously impaired, non-core equity security, since it is now more likely than not that such benefit will be realized.

For the thirteen weeks ended February 26, 2005, the Company's effective tax rate of 10% differed from the Federal statutory tax rate of 34% due primarily to the reversal of a valuation allowance relating to a previously impaired, non-core equity security sold during the period and losses of a U.S. subsidiary which operated in Puerto Rico, partially offset by non-deductible expenses. For the thirty-nine weeks ended February 26, 2005, the Company's effective tax rate of 11% differed from the Federal statutory tax rate of 34% due primarily to the reversal of a valuation allowance relating to a previously impaired, non-core equity security sold during the period and losses of a U.S. subsidiary which operated in Puerto Rico,



E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE J INCOME TAXES (continued)**

partially offset by non-deductible expenses, including stock option compensation costs of \$377,000.

**NOTE K CONTINGENCIES**

**Litigation Matters**

The Company was named as a co-defendant in an action entitled Jeffrey Madison d/b/a Maqguide.com vs. Avail Medical Products, Inc. et al., Case No. 05CC03584 filed in Superior Court for the State of California, Orange County, on February 28, 2005. The complaint alleges that in March 2003, the Company sought a contract manufacturer to manufacture and supply certain medical products and the Company, acting through its agent, Sopheon Corporation, solicited Maqguide to assist in this process. The complaint alleges that, acting on this information, Maqguide contacted Avail Medical Products, Inc., or Avail, about this opportunity and helped negotiate a final agreement between the Company and Avail. The complaint further alleges that Maqguide had an agreement with Avail that required Avail to pay a commission to Maqguide upon the execution of the agreement with the Company. The complaint alleges 18 causes of action against all of the defendants, including breach of contract, breach of the covenant of good faith, quantum meruit, fraud and deceit, promissory estoppel, conspiracy and conversion. The complaint seeks compensatory, punitive and other monetary damages in an unspecified amount in excess of \$25,000. The Company has engaged counsel to defend this matter and believes that the allegations against it are without merit and intends to vigorously defend this action.

AngioDynamics and E-Z-EM were named as co-defendants in an action entitled Duhon, et. al vs. Brezoria Kidney Center, Inc. et. al, case no. 27084 filed in the District Court of Brezoria County, Texas, 239<sup>th</sup> Judicial District on December 29, 2003. The complaint alleged that AngioDynamics and its co-defendants, E-Z-EM and Medical Components, Inc. or Medcomp, designed, manufactured, sold, distributed and marketed a defective catheter that was used in the treatment of, and caused the death of, a hemodialysis patient, as well as committed other negligent acts. The complaint sought compensatory and other monetary damages in unspecified amounts. Under AngioDynamics' distribution agreement with Medcomp, Medcomp was required to indemnify AngioDynamics against all its costs and expenses, as well as losses, liabilities and expenses (including reasonable attorneys' fees) that relate in any way to products covered by the agreement, and Medcomp accepted the defense of the action. This matter has been settled and an order for dismissal with prejudice was entered into the court on August 5, 2005.

E-Z-EM, Inc. and Subsidiaries

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 4, 2006 and February 26, 2005

(unaudited)

**NOTE K CONTINGENCIES (continued)**

In accordance with the Master Separation and Distribution Agreement between AngioDynamics and E-Z-EM, AngioDynamics has agreed to indemnify E-Z-EM against any claims that arise out of the business operations of AngioDynamics prior to its spin-off (October 30, 2004) in which E-Z-EM is a named defendant solely because E-Z-EM was the sole stockholder of AngioDynamics.

The Company is party to other claims, legal actions and complaints that arise in the ordinary course of business. The Company believes that any liability that may ultimately result from the resolution of these matters will not, individually or in the aggregate, have a material adverse effect on its financial position or results of operations.

**Other Matters**

During 2004, the Company was notified by a competitor that it believed specific claims contained in issued United States patents owned by this competitor may be relevant to certain features of the Company's electromechanical injector systems. In August 2005, the Company entered into a licensing arrangement covering the design and form of its injector systems as of the date of such agreement. At May 28, 2005, the Company recorded an estimated liability in this matter of \$350,000 that the Company believes relieved it of all claims relating to prior sales.

**Concentration of Credit Risk**

In November 2005, Merry X-Ray Corporation ( Merry X-Ray ), a significant distributor of the Company's products in the U.S., acquired SourceOne Healthcare Technologies, Inc. ( SourceOne ), the Company's largest distributor in the U.S. For the forty weeks ended March 4, 2006 and the thirty-nine weeks ended February 26, 2005, sales of products to Merry X-Ray, including sales to SourceOne before its acquisition by Merry X-Ray, represented 37% and 38% of total sales, respectively. Approximately 39% of accounts receivable pertained to Merry X-Ray at

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March 4, 2006 and approximately 6% and 31% of accounts receivable pertained to Merry X-Ray and SourceOne, respectively, at May 28, 2005. While the accounts receivable related to Merry X-Ray are significant, the Company does not believe the credit risk to be significant given the consistent payment history of this distributor.

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E-Z-EM, Inc. and Subsidiaries

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 4, 2006 and February 26, 2005

(unaudited)

#### NOTE L - COMMON STOCK

##### Stock Repurchase Program

In March 2003, the Board of Directors authorized the repurchase of up to 300,000 shares of the Company's common stock at an aggregate purchase price of up to \$3,000,000. During the forty weeks ended March 4, 2006, no shares were repurchased under this program. In aggregate, the Company has repurchased 74,234 shares of common stock for approximately \$716,000 under this program.

##### Cash Dividends

In June 2004, the Company's Board of Directors declared a cash dividend of \$.30 per outstanding share of the Company's common stock. The dividend, which aggregated \$3,220,000, was distributed on July 1, 2004 to shareholders of record as of June 15, 2004. Future dividends are subject to Board of Directors' review of operations and financial and other conditions then prevailing.

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Item 2. **Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following information should be read together with the consolidated financial statements and the notes thereto and other information included elsewhere in this Quarterly Report on Form 10-Q.

**Forward-Looking Statements and Risk Factors**

Our disclosure and analysis in this report, including but not limited to the information discussed in this Item 2, contain forward-looking information about our company's financial results and estimates, business prospects and products in research that involve substantial risks and uncertainties. From time to time, we also may provide oral or written forward-looking statements in other materials we release to the public. Forward-looking statements give our current expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historic or current facts. They use words such as anticipate, estimate, expect, project, intend, plan, believe, will, words and terms of similar meaning in connection with any discussion of future operations or financial performance. In particular, these include statements relating to future actions, prospective products or product approvals, future performance or results of current and anticipated products, sales efforts, expenses, interest rates, foreign exchange rates, the outcome of contingencies, such as legal proceedings, and financial results. Among the risk factors that could cause actual results to differ materially are the following:

our pricing flexibility is constrained by the formation of large Group Purchasing Organizations;

our complete reliance on our Canadian manufacturing facility to produce substantially all of our CT and X-ray fluoroscopy barium sulfate formulation products may impair our ability to respond to natural disasters or other adverse events, and also exposes us to the effects of changes in Canadian dollar U.S. dollar exchange rate;

we currently purchase significant amounts of finished products, product components and raw materials from several single-source suppliers;

the market dynamics and competitive environment in the healthcare industry are subject to rapid change, which may affect our operations;

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if third parties claim that our products infringe their intellectual rights, we may be forced to expend significant financial resources and management time defending against such actions and our results of operations could suffer;

we sell our products in the U.S. through a network of approximately 150 distributors, although one distributor accounted for approximately 37% of our net sales in fiscal 2005, which exposes us to a concentration of credit risk;

the market potential for our Reactive Skin Decontamination Lotion product is uncertain and sales in this market are subject to complex governmental procedures;

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if we fail to develop new products and enhance existing products, we could lose market share to our competitors and our results of operations could suffer;

if we fail to adequately protect our intellectual property rights, our business may suffer;

the adoption rate of virtual colonoscopy as a screening modality for colon cancer continues to be slower than we anticipated;

if we cannot obtain approval from governmental agencies for new or modified products, we will not be able to sell those products;

inadequate levels of reimbursement from governmental or other third-party payors for procedures using our products may cause our revenues to decline; and

if we incur a tax liability in connection with our spin-off of AngioDynamics, we would incur a potentially significant expense, which would diminish our financial resources.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from past results and those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements.

You are advised to consult any further disclosures we make on related subjects in our Forms 10-Q, 8-K and 10-K reports to the Securities and Exchange Commission. Our Form 10-K filing for the 2005 fiscal year listed various important factors that could cause actual results to differ materially from expected and historic results. We note these factors for investors as permitted by the Private Securities Litigation Reform Act of 1995. Readers can find them in Item 7 of that filing under the heading Risk Factors. You should understand that it is not possible to predict or identify all such factors. Consequently, you should not consider any such list to be a complete set of all potential risks or uncertainties.

**Overview**

We are a leading provider of medical diagnostic oral contrast agents and devices used in the diagnosis of abdominal disease. Our customers include radiologists and gastroenterologists. We are focused on becoming a worldwide CT solutions company for the computed tomography (CT) market. This focus is driven by the trend away from older fluoroscopic procedures (e.g., barium enema) to CT-based applications for imaging the abdominal tract.

We have pioneered solutions for the emerging area of Virtual Colonography, which may offer unique capabilities for the early detection of colorectal cancer, and have also developed new contrast agents (e.g., VoLumen) that focus on CT and CT Angiography applications in Multidetector CT technology. We also manufacture and market a line of CT power injectors, which are used to deliver CT contrast agents. Our Empower CT injector was recently rated number one in user satisfaction among vendors of CT power injectors by MD Buyline, a leading market research and analysis publisher covering the healthcare industry.

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In November, we introduced our IRiSCT™ software technology at the Radiological Society of North America convention. We believe this software platform is the first contrast information management system to be brought to market, and that it will enhance both the clinical and operational efficiency of our CT power injectors. The platform allows for multiple Empower CT power injectors to be networked to a central computer database. Injector performance and contrast utilization data is collected on a real-time basis and is automatically transferred to a central database for remote review. This information can be used to evaluate and quantify the clinical aspects of the injector's performance, thus enabling more effective and productive use in treating patients.

In addition to our products for the radiology market, we have continued to focus our efforts in the area of defense decontaminants. Reactive Skin Decontamination Lotion (RSDL) is a liquid skin decontaminant that is effective in neutralizing a broad spectrum of chemical warfare and toxic agents. On April 7, 2005, we purchased from our strategic partner, O'Dell Engineering, all its assets related to the RSDL technology. We now have exclusive, worldwide rights to the RSDL technology for the military and first-responder markets. Prior to the acquisition, we were the exclusive manufacturer of RSDL under an agreement between O'Dell Engineering and our Canadian subsidiary. We are continuing to staff key positions for our RSDL product team.

In mid-December 2004, our principal competitor, Mallinckrodt, a division of Tyco International Ltd., initiated a recall of its liquid barium products due to potential microbial contamination. As a result, our net sales have been favorably affected by our ability to provide replacement products during the past five fiscal quarters. In the fourth quarter of our fiscal 2005, Mallinckrodt returned to market with one of their products. Subsequent to the third quarter of our fiscal 2006, Mallinckrodt began to supply several additional products to the market and we expect them to return with their remaining products shortly. We are unable to predict the extent of the effect that Mallinckrodt's return to the market will have on our business.

In February 2006, the Executive Committee of our Board of Directors approved a plan to wind down and close the operations of Toho Kagaku Kenkyusho Co., Ltd. ( Toho ), a wholly owned Japanese subsidiary. The decision to close Toho resulted from an inability to generate income from operations and to grow the business due to a limited product offering and scope of operations. Also, a recent change in manufacturing location required a re-registration of Toho's principal products with Japanese regulatory authorities, resulting in a projected interruption of supply during the first quarter of fiscal 2007. Management plans a market withdrawal on a staged basis so that current inventory can be sold, accounts receivable collected and the property sold in an organized fashion, while also satisfying all outstanding liabilities.

### **Results of Operations**

#### **Quarters ended March 4, 2006 and February 26, 2005**

Our quarters ended March 4, 2006 and February 26, 2005 both represent thirteen weeks.

### **Consolidated Results of Operations**

For the quarter ended March 4, 2006, we reported net earnings of \$4,342,000, or \$.40 and \$.39 per common share on a basic and diluted basis, respectively, as compared to net earnings of \$2,918,000, or \$.27 per common share on both a

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basic and diluted basis, for the comparable period of last year. Results for the current quarter included a tax benefit of \$2,347,000, or \$.22 per basic share, associated with the closing of our Japanese subsidiary. Results for the current quarter also included the reversal of a tax valuation allowance of \$496,000, or \$.05 per basic share, relating to a previously impaired, non-core equity security.

Operating results for the current quarter were favorably affected by increased sales and gross profit and decreased operating expenses. The decline in operating expenses was due to the recognition of a \$1,205,000 gain on the sale of our former manufacturing facility in Westbury, N.Y. This sale was the culmination of the plan to relocate our powder-based barium production from Westbury to our manufacturing facility in Montreal, Canada. Results for the current quarter also included \$257,000 in plant closing and operational restructuring costs incurred in winding down and closing our Japanese facility and a \$39,000 credit associated with the relocation of our powder-based barium production. Results for the comparable quarter of last year included \$649,000 in plant closing and operational restructuring costs incurred in connection with the relocation of our powder-based barium production.

Our operating results are expressed as a percentage of net sales in the following table:

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	Thirteen weeks ended	
	March 4, 2006	February 26, 2005
Net sales	100.0%	100.0%
Cost of goods sold	60.4	58.7
<b>Gross profit</b>	<b>39.6</b>	<b>41.3</b>
Operating expenses		
Selling and administrative	31.3	29.0
Plant closings and operational restructuring costs	0.7	2.1
Gain on sale of real property	(3.7)	
Research and development	4.8	4.6
<b>Total operating expenses</b>	<b>33.1</b>	<b>35.7</b>
<b>Operating profit</b>	<b>6.5</b>	<b>5.6</b>
Other income (expense)		
Interest income	0.7	0.3
Interest expense	(0.3)	(0.3)
Other, net	0.5	4.9
<b>Earnings before income taxes</b>	<b>7.4</b>	<b>10.5</b>
Income tax provision (benefit)	(6.1)	1.0
<b>NET EARNINGS</b>	<b>13.5%</b>	<b>9.5%</b>

Net sales for the quarter ended March 4, 2006 increased 5%, or \$1,432,000, as compared to the quarter ended February 26, 2005, due to organic sales growth and, to a lesser extent, price increases, which accounted for 1% of net sales for the current period, as a significant portion of our domestic products are



sold under long-term group purchasing organization contracts. On a product line basis, the net sales increase resulted primarily from increased sales of CT injector systems of \$1,567,000 and contract manufacturing products of \$1,338,000, partially offset by a decline in sales of X-ray fluoroscopy products of \$907,000 and CT imaging contrast products of \$724,000. The decline in sales of X-ray fluoroscopy and CT imaging contrast products was due primarily to the consolidation of our two largest U.S. distributors resulting in lower levels of on-hand inventory.

Net sales in international markets, including direct exports from the U.S., increased 13%, or \$1,306,000, for the current quarter from the prior year's quarter due to increased sales of contract manufacturing products of \$742,000, CT imaging products of \$385,000 and all other products of \$179,000.

The following table sets forth net sales by product category for the quarters ended March 4, 2006 and February 26, 2005:

	2006		2005	
	\$	%	\$	%
(dollars in thousands)				
CT Imaging Contrast	\$ 7,793	24.1	\$ 8,517	27.6
CT Injector Systems	5,871	18.2	4,304	14.0
Total CT Imaging	13,664	42.3	12,821	41.6
X-Ray Fluoroscopy	10,079	31.2	10,986	35.6
Contract Manufacturing	4,005	12.4	2,667	8.7
Accessory Medical Devices	1,315	4.1	1,324	4.3
Gastroenterology	1,205	3.7	1,064	3.5
Virtual Colonoscopy	985	3.1	968	3.1
Defense Decontaminants	122	0.4	226	0.7
Other	890	2.8	777	2.5
	\$ 32,265	100.0	\$ 30,833	100.0

Gross profit, expressed as a percentage of net sales, decreased to 40% for the current quarter from 41% for the comparable quarter of the prior year due to increased materials cost primarily from our barium sulfate suppliers and increased costs associated with purchased finished products, partially offset by sales price increases. Increased finished product costs resulted primarily from finished goods purchased from our Canadian subsidiary, which were adversely affected by the continued weakening of the U.S. dollar against the Canadian dollar. Our third fiscal quarters historically have fewer production days than the other fiscal quarters, resulting in somewhat lower gross profit percentages.

Selling and administrative ( S&A ) expenses were \$10,094,000 for the quarter ended March 4, 2006, compared to \$8,923,000 for the quarter ended February 26, 2005. This increase of \$1,171,000, or 13%, was due primarily to additional infrastructure expenses of \$520,000 to support our defense decontaminants business and increased compensation costs, including fringe benefits, of \$421,000.

Research and development ( R&D ) expenditures remained at 5% of net sales and increased 10% for the current quarter to \$1,563,000 from \$1,421,000 for the comparable quarter of the prior year, due primarily to increased costs of \$234,000 for X-ray fluoroscopy and CT imaging projects, partially offset by decreased spending in all other areas of R&D. Of the R&D expenditures for the current quarter, approximately 63% related to X-ray fluoroscopy and CT imaging projects, 26% to general regulatory costs, 7% to gastroenterology

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projects and 4% to other projects. R&D expenditures are expected to continue at approximately current levels.

Other income and expenses totaled \$276,000 of income for the current quarter compared to \$1,495,000 of income for the comparable period of last year. The comparable period of last year included a gain of \$979,000 on the sale of a non-core equity security and foreign currency exchange gains of \$461,000.

For the quarter ended March 4, 2006, we reported an income tax benefit of \$1,958,000 against earnings from continuing operations before income taxes of \$2,384,000 due primarily to: i) a tax benefit of \$2,347,000 associated with the closing of our Japanese subsidiary; and ii) the reversal of a valuation allowance of \$496,000 relating to a previously impaired, non-core equity security, since it is now more likely than not that such benefit will be realized. For the quarter ended February 26, 2005, our effective tax rate of 10% differed from the Federal statutory tax rate of 34% due primarily to the reversal of a valuation allowance relating to a previously impaired, non-core equity security sold during the quarter and losses of a U.S. subsidiary which operated in Puerto Rico, partially offset by non-deductible expenses.

#### **Nine months ended March 4, 2006 and February 26, 2005**

Our nine months ended March 4, 2006 and February 26, 2005 represent forty weeks and thirty-nine weeks, respectively.

#### **Consolidated Results of Operations**

For the nine months ended March 4, 2006, we reported net earnings of \$8,420,000, or \$.78 and \$.76 per common share on a basic and diluted basis, respectively, compared to net earnings of \$5,600,000, or \$.52 and \$.51 per common share on a basic and diluted basis, respectively, for the comparable period of last year. Results for the current period included a tax benefit of \$2,347,000, or \$.22 per basic share, associated with the closing of our Japanese subsidiary. Results for the current period also included the reversal of a tax valuation allowance of \$496,000, or \$.05 per basic share, relating to a previously impaired, non-core equity security.

The following table sets forth earnings from continuing operations and earnings from discontinued operation:

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	Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	(in thousands)	
Earnings from continuing operations	\$ 8,420	\$ 4,372
Earnings from discontinued operation		1,228
Net earnings	\$ 8,420	\$ 5,600

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Our operating results are expressed as a percentage of net sales in the following table:

	Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
Net sales	100.0%	100.0%
Cost of goods sold	56.6	57.3
Gross profit	43.4	42.7
Operating expenses		
Selling and administrative	31.5	32.3
Plant closings and operational restructuring costs	0.3	2.6
Gain on sale of real property	(1.2)	
Research and development	4.3	4.8
Total operating expenses	34.9	39.7
Operating profit	8.5	3.0

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	Forty weeks ended March 4, 2006	Thirty-nine weeks ended February 26, 2005
	<u>          </u>	<u>          </u>
Other income (expense)		
Interest income	0.5	0.3
Interest expense	(0.3)	(0.3)
Other, net	(0.2)	3.1
	<u>          </u>	<u>          </u>
Earnings from continuing operations before income taxes	8.5	6.1
Income tax provision	0.2	0.7
	<u>          </u>	<u>          </u>
Earnings from continuing operations	8.3	5.4
Earnings from discontinued operation, net of income tax provision		1.5
	<u>          </u>	<u>          </u>
NET EARNINGS	8.3%	6.9%
	<u>          </u>	<u>          </u>

**Continuing Operations**

Operating results for the current period were favorably affected by increased sales and improved gross profit, partially offset by increased operating expenses. Results for the current period included a gain of \$1,205,000 on the sale of our former manufacturing facility in Westbury, N.Y. This sale was the culmination of the plan to relocate our powder-based barium production from Westbury to our manufacturing facility in Montreal, Canada. Results for the current period also included \$257,000 in plant closing and operational restructuring costs incurred in winding down and closing our Japanese facility and \$96,000 in costs associated with the relocation of our powder-based barium production. Results for the comparable quarter of last year included \$2,074,000 in plant closing and operational restructuring costs incurred in connection with the relocation of our powder-based barium production.

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Net sales for the nine months ended March 4, 2006 increased 25%, or \$20,186,000, compared to the nine months ended February 26, 2005, due to organic sales growth, the Mallinckrodt liquid barium product recall, and the additional week in the current reporting period. The increase in

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net sales attributable to the Mallinckrodt recall affected both CT imaging and X-ray fluoroscopy product categories. Price increases accounted for less than 2% of net sales for the current period, as a significant portion of our domestic products are sold under long-term group purchasing organization contracts. On a product line basis, the net sales increase resulted from increased sales of CT imaging contrast products, particularly our CT Smoothie lines, and CT injector systems, totaling \$11,189,000, X-ray fluoroscopy products of \$3,506,000, contract manufacturing products of \$2,818,000 and all other products of \$2,673,000.

Net sales in international markets, including direct exports from the U.S., increased 20%, or \$5,498,000, for the current period from the comparable prior year period due to increased sales of defense decontaminants of \$1,576,000, contract manufacturing products of \$1,090,000, CT imaging products of \$1,069,000, X-ray fluoroscopy products of \$828,000, virtual colonoscopy products of \$583,000 and all other products of \$352,000.

The following table sets forth net sales by product category for the nine months ended March 4, 2006 and February 26, 2005:

	2006		2005	
	\$	%	\$	%
	(dollars in thousands)			
CT Imaging Contrast	\$ 27,051	26.7	\$ 19,931	24.6
CT Injector Systems	16,704	16.5	12,635	15.6
	43,755	43.2	32,566	40.2
X-Ray Fluoroscopy	33,959	33.5	30,453	37.6
Contract Manufacturing	8,140	8.1	5,322	6.6
Accessory Medical Devices	4,059	4.0	3,991	4.9
Gastroenterology	3,743	3.7	3,337	4.1
Virtual Colonoscopy	2,892	2.9	2,721	3.3
Defense Decontaminants	1,936	1.9	467	0.6
Other	2,769	2.7	2,210	2.7
	\$ 101,253	100.0	\$ 81,067	100.0

Gross profit, expressed as a percentage of net sales, was 43% for both the current period and the comparable period of the prior year. Favorable changes in sales product mix and sales price increases, including the effects of lower distributor rebates as a percentage of sales, offset increased materials cost primarily from our barium sulfate suppliers and increased costs associated with purchased finished products. Favorable changes in sales product mix can be attributed, in part, to the increased sales resulting from the Mallinckrodt recall. Increased finished product costs resulted primarily from finished goods purchased from our Canadian subsidiary which were adversely affected by the continued weakening of the U.S. dollar against the Canadian dollar.

S&A expenses were \$31,909,000 for the nine months ended March 4, 2006 compared to \$26,192,000 for the nine months ended February 26, 2005. This increase of \$5,717,000, or 22%, was due, in large part, to: i) increased compensation costs, including fringe benefits, of \$2,080,000; ii) additional infrastructure expenses of \$1,638,000 to support our defense decontaminants business; and iii) increased selling expenses relating to the increase in net sales. The comparable period of the prior year included a non-cash

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compensation charge of \$406,000 resulting from the modification of certain stock options previously granted to one of our former directors.

R&D expenditures increased 10% for the current period to \$4,318,000, or 4% of net sales, from \$3,919,000, or 5% of net sales, for the comparable period of the prior year due primarily to increased costs of \$612,000 for X-ray fluoroscopy and CT imaging projects and increased general regulatory costs of \$221,000, partially offset by decreases in spending of \$212,000 for virtual colonoscopy projects and \$194,000 for gastroenterology projects. Of the R&D expenditures for the current period, approximately 58% related to X-ray fluoroscopy and CT imaging projects, 30% to general regulatory costs, 8% to gastroenterology projects and 4% to other projects.

Other income and expenses totaled \$22,000 of income for the current period compared to \$2,503,000 of income for the comparable period of last year. The comparable period of last year included gains of \$2,385,000 on the sales of a non-core equity security.

For the nine months ended March 4, 2006, our unusually low effective tax rate of 2% differed from the Federal statutory tax rate of 34% due primarily to: i) a tax benefit of \$2,347,000 associated with the closing of our Japanese subsidiary; and ii) the reversal of a valuation allowance of \$496,000 relating to a previously impaired, non-core equity security, since it is now more likely than not that such benefit will be realized. For the nine months ended February 26, 2005, our effective tax rate of 11% differed from the Federal statutory tax rate of 34% due primarily to the reversal of a valuation allowance relating to a previously impaired, non-core equity security sold during the period and losses of a U.S. subsidiary which operated in Puerto Rico, partially offset by non-deductible expenses, including stock option compensation costs of \$377,000.

### **Discontinued Operations**

We have consolidated the financial statements of AngioDynamics and reported its results as a discontinued operation in an amount equal to our percentage of equity ownership through October 30, 2004, the date on which our spin-off of AngioDynamics was completed. Since the spin-off occurred in the second quarter of our prior fiscal year, the results for the discontinued operation were excluded from the accompanying consolidated statement of earnings for the current period.

Summarized results of operations for AngioDynamics, including minority interest, as reported in earnings from discontinued operation in the accompanying consolidated statement of earnings for the thirty-nine weeks ended February 26, 2005 are as follows (amounts in thousands):

Net sales	
From unaffiliated customers	\$ 22,342
From affiliates	420
	<hr/>
Total net sales	\$ 22,762
	<hr/>
Earnings before income taxes and minority interest	
	\$ 2,628
Income tax provision	1,103
	<hr/>
Earnings before minority interest	1,525
Minority interest	297
	<hr/>
Earnings from discontinued operation	\$ 1,228
	<hr/>

For the thirty-nine weeks ended February 26, 2005, the results of operations for AngioDynamics represented twenty-two weeks activity.

**Liquidity and Capital Resources**

For the nine months ended March 4, 2006, operations, capital expenditures and an advanced royalty fee were funded by working capital and proceeds from the sale of assets. Our policy has generally been to fund operations and capital requirements without incurring significant debt. As of March 4, 2006, debt (notes payable, current maturities of long-term debt and long-term debt) was \$273,000, as compared to \$531,000 at May 28, 2005. We have available \$1,762,000 under a bank line of credit, of which no amounts were outstanding at March 4, 2006.

Our contractual obligations and their effect on liquidity and cash flows as of March 4, 2006 are set forth in the table below. We have no variable interest entities or other off-balance sheet obligations.

**Payments Due By Period as of March 4, 2006**

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**Total**

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Payments Due By Period as of March 4, 2006

	Less than 1 year	1-3 years	3-5 years	More than 5 years
(in thousands)				
<b>Contractual Obligations:</b>				
Long-term debt	\$ 103	\$ 80	\$ 23	
Notes payable	170	170		
Operating leases (1)	7,568	1,788	3,358	\$ 2,378 \$ 44
Purchase obligations (1)	3,052	2,903	149	
Employment contract (1)	680	680		
Consulting contracts (1)	35	35		
Other long-term liabilities reflected on the consolidated balance sheet				
Deferred compensation (2)	2,670	19	45	57 2,549
Asset acquisition	1,400	700	700	
License arrangements	1,013	795	218	
Accrued retirement benefits	178	178		
<b>Total</b>	<b>\$ 16,869</b>	<b>\$ 7,348</b>	<b>\$ 4,493</b>	<b>\$ 2,435 \$ 2,593</b>

(1) The non-cancelable operating leases, purchase obligations, and employment and consulting contracts are not reflected on the consolidated balance sheet under accounting principles generally accepted in the United States of America. The purchase obligations consist primarily of finished good product and component parts.

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(2) Deferred compensation costs covering active employees are assumed payable after five years, although certain circumstances, such as termination, would require earlier payment.

At March 4, 2006, approximately \$31,687,000, or 27%, of our assets consisted of cash and cash equivalents and short-term debt and equity securities. The current ratio was 5.77 to 1, with net working capital of \$74,086,000, at March 4, 2006, compared to the current ratio of 4.81 to 1, with net working capital of \$59,612,000, at May 28, 2005. The increase in working capital is due, in large part, to increased inventory of \$4,640,000, to support our increased business, and increased accounts receivable of \$4,861,000, resulting from increased sales. We believe that our cash reserves, cash provided from continuing operations and existing bank line of credit will provide sufficient liquidity to meet our current obligations for the next 12 months.

In March 2003, the Board of Directors authorized the repurchase of up to 300,000 shares of our common stock at an aggregate purchase price of up to \$3,000,000. During the nine months ended March 4, 2006, no shares were repurchased under this program. In aggregate, we have



repurchased 74,234 shares of common stock for approximately \$716,000 under this program.

In June 2004, our Board of Directors declared a cash dividend of \$.30 per outstanding share of our common stock. The dividend, which aggregated \$3,220,000, was distributed on July 1, 2004 to shareholders of record as of June 15, 2004. Future dividends are subject to our Board of Directors' review of operations and financial and other conditions then prevailing.

### **Critical Accounting Policies**

Our significant accounting policies are summarized in Note A to the Consolidated Financial Statements included in our Annual Report on Form 10-K for our fiscal year ended May 28, 2005. While all these significant accounting policies affect the reporting of our financial condition and results of operations, we view certain of these policies as critical. Policies determined to be critical are those policies that have the most significant impact on our financial statements and require us to use a greater degree of judgment and/or estimates. Actual results may differ from those estimates.

We believe that given current facts and circumstances, it is unlikely that applying any other reasonable judgment or estimate methodologies would cause a material effect on our consolidated results of operations, financial position or liquidity for the periods presented in this report. The accounting policies identified as critical are as follows:

### **Revenue Recognition**

We recognize revenues in accordance with generally accepted accounting principles as outlined in Staff Accounting Bulletin No. 104, Revenue Recognition in Financial Statements, which requires that four basic criteria be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) the price is fixed or determinable; (3) collectibility is reasonably assured; and (4) product delivery has occurred or services have been rendered. Decisions relative to criterion (3) regarding collectibility are based upon our judgments, as discussed under Accounts Receivable below, and should conditions change in the future and cause us to determine this criterion is not met, our results of operations may be affected. We recognize revenue on the date the product is shipped, which is

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when title passes to the customer. Shipping and credit terms are negotiated on a customer-by-customer basis. Products are shipped primarily to distributors at an agreed upon list price. The distributor then resells the products primarily to hospitals and, depending upon contracts between us, the distributor and the hospital, the distributor may be entitled to a rebate. We deduct all rebates from sales and have a provision for rebates based on historical information for all rebates that have not yet been submitted to us by the distributors.

Changes in our rebate allowance for the nine months ended March 4, 2006 are as follows (amounts in thousands):

Beginning balance	\$ 1,397
Provision for rebates	19,260
Rebate credits issued	(18,936)
	<hr/>
Ending balance	\$ 1,721
	<hr/>

The rebate allowance is comprised of three components:

actual rebate requests received from distributors prior to the closing of our financial statements;

an estimate, compiled by distributor, of rebate requests not yet received based on historical submissions, adjusted for any material changes in purchasing patterns or market conditions; and

an estimate of distributors' inventory-on-hand available for future sale pursuant to a group purchasing organization ( GPO ) contract. We do not have visibility as to the specific inventory levels held by our distributors. However, based on discussions with our customers, who uniformly attempt to maintain a just-in-time purchasing program, and our knowledge of their ordering patterns, we estimate a one-week wholesale inventory level. Since most of our product sales are subject to GPO contracts, most distributor inventory-on-hand will be subject to rebate. This portion of the rebate estimate is derived by first determining the total quantity of each product sold by us during the last week of the fiscal period multiplied by two factors, (a) and (b), where (a) is the percentage of each product rebated during the prior six-month period based on historical sales and (b) is the average rebate paid on that product during this period.

All product returns must be pre-approved by us and may be subject to a 20% restocking charge. To be accepted, a returned product must be unadulterated, undamaged and must have at least 12 months remaining on its stated expiration date.

We record revenue on warranties and extended warranties on a straight-line basis over the term of the related warranty contracts, which generally cover one year. Deferred revenues related to warranties and extended warranties were \$531,000 and \$505,000 at March 4, 2006 and May 28, 2005, respectively. Service costs are expensed as incurred.

#### Accounts Receivable

Accounts receivable are generally due within 30 to 90 days and are stated at amounts due from customers, net of an allowance for doubtful accounts. We perform ongoing credit evaluations and adjust credit limits based upon payment history and the customer's current credit worthiness, as determined by a review of their current credit information. We continuously monitor

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aging reports, collections and payments from customers, and maintain a provision for estimated credit losses based upon historical experience and any specific customer collection issues we identify. While such credit losses have historically been within expectations and the provisions established, we cannot guarantee the same credit loss rates will be experienced in the future. We write off accounts receivable when they become uncollectible. At March 4, 2006 and May 28, 2005, our allowance for doubtful accounts was \$887,000 and \$869,000, respectively. Concentration risk exists relative to our accounts receivable, as 39% of our total accounts receivable balance at March 4, 2006 is concentrated in one distributor. While the accounts receivable related to this distributor are significant, we do not believe the credit risk to be significant given the distributor's consistent payment history.

Changes in our allowance for doubtful accounts for the nine months ended March 4, 2006 are as follows (amounts in thousands):

Beginning balance	\$	869
Provision for doubtful accounts		45
Write-offs		(27)
		<hr/>
Ending balance	\$	887
		<hr/>

### Income Taxes

In preparing our financial statements, income tax expense is calculated for each jurisdiction in which we operate. This involves estimating actual current taxes due plus assessing temporary differences arising from differing treatment for tax and accounting purposes that are recorded as deferred tax assets and liabilities. Deferred tax assets are periodically evaluated to determine their recoverability, based primarily on our ability to generate future taxable income. Where their recovery is not likely, we establish a valuation allowance and record a corresponding additional tax expense in our statement of earnings. If actual results differ from our estimates due to changes in assumptions, the provision for income taxes could be materially affected.

### Inventories

We value inventories at the lower of cost (on the first-in, first-out method) or market. On a quarterly basis, we review inventory quantities on hand and analyze the provision for excess and obsolete inventory based primarily on product expiration dating and our estimated sales forecast, which is based on sales history and anticipated future demand. Our estimates of future product demand may not be accurate and we may understate or overstate the provision required for excess and obsolete inventory. Accordingly, any significant unanticipated changes in demand could have a significant impact on the value of our inventory and results of operations. At March 4, 2006 and May 28, 2005, our reserve for excess and obsolete inventory was \$1,912,000 and \$1,902,000, respectively.

### Property, Plant and Equipment

We state property, plant and equipment at cost, less accumulated depreciation, and depreciate principally using the straight-line method over their estimated useful lives. We determine this based on our estimates of the period over which the asset will generate revenue. Any change in condition that would cause us to change our estimate of the useful lives of a

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group or class of assets may significantly affect depreciation expense on a prospective basis.

### **Effects of Recently Issued Accounting Pronouncements**

In March 2004, the Financial Accounting Standards Board ( FASB ) Emerging Issues Task Force ( EITF ) released Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. EITF 03-1 provides guidance for determining whether impairment for certain debt and equity investments is other-than-temporary and the measurement of an impaired loss. Certain disclosure requirements of EITF 03-1 were adopted in fiscal 2004 and we have complied with the new disclosure requirements in our consolidated financial statements. The recognition and measurement requirements of EITF 03-1 were initially effective for reporting periods beginning after June 15, 2004. In September 2004, the FASB Staff issued FASB Staff Position ( FSP ) EITF 03-1-1 that delayed the effective date for certain measurement and recognition guidance contained in EITF 03-1. The FSP requires that entities continue to apply previously existing other-than-temporary guidance until a final consensus is reached. We do not anticipate that the issuance of a final consensus will materially impact our financial condition or results of operations.

In November 2004, the FASB issued Statement of Financial Accounting Standards ( SFAS ) No. 151, Inventory Costs , an amendment of ARB No. 43, Chapter 4. The amendments made by SFAS No. 151 will improve financial reporting by clarifying that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and by requiring the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 24, 2004. The adoption of this statement is not expected to have a material impact on our financial condition or results of operations.

In December 2004, the FASB issued SFAS No. 123 (R), Share-Based Payment , which revises SFAS No. 123, Accounting for Stock-Based Compensation and supercedes APB Opinion No. 25, Accounting for Stock Issued to Employees . SFAS No. 123 (R) establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. This statement focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. SFAS No. 123 (R) requires that the fair value of such equity instruments be recognized as an expense in the historical financial statements as services are performed. Prior to SFAS No. 123 (R), only certain pro forma disclosures of fair value were required. In April 2005, the Securities and Exchange Commission adopted a new rule that amended the compliance dates of SFAS No. 123 (R) to require the implementation no later than the beginning of the first annual reporting period beginning after June 15, 2005. The adoption of this statement may have a material impact on our financial condition and results of operations commencing with the fiscal quarter ending September 2, 2006.

On December 31, 2004, the FASB issued FASB Staff Position No. FAS 109-2, Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004, ( FSP No. 109-2 ). This staff position provides accounting guidance on how companies should account for the effects of the American Jobs Creation Act of 2004 ( AJCA ) that was signed into law on October 22, 2004.

FSP No. 109-2 gives a company additional time to evaluate the effects of the legislation on any plan for

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reinvestment or repatriation of foreign earnings for purposes of applying FASB Statement No. 109. We are investigating the repatriation provision to determine whether we might repatriate extraordinary dividends, as defined in the AJCA. We are currently evaluating all available U.S. Treasury guidance.

In June 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, a replacement of APB Opinion No. 20, *Accounting Changes*, and FASB Statement No. 3, *Reporting Accounting Changes in Interim Financial Statements*. SFAS No. 154 changes the requirements for the accounting for and reporting of a change in accounting principle. Previously, most voluntary changes in accounting principles required recognition via a cumulative effect adjustment within net income for the period of the change. SFAS No. 154 requires retrospective application to prior periods' financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. SFAS No. 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005; however, SFAS No. 154 does not change the transition provisions of any existing accounting pronouncements. We do not believe the adoption of SFAS No. 154 will have a material impact on our financial condition or results of operations.

Item 3. **Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to market risk from changes in foreign currency exchange rates and, to a much lesser extent, interest rates on investments and financing, which could impact our results of operations and financial position. We do not currently engage in any hedging or market risk management tools. There have been no material changes with respect to market risk previously disclosed in our Annual Report on Form 10-K for our 2005 fiscal year.

**Foreign Currency Exchange Rate Risk**

The financial reporting of our international subsidiaries is denominated in currencies other than the U.S. dollar. Since the functional currency of our international subsidiaries is the local currency, foreign currency translation adjustments are accumulated as a component of accumulated other comprehensive income in stockholders' equity. Assuming a hypothetical aggregate change in the exchange rates of foreign currencies against the U.S. dollar of 10% at March 4, 2006, our assets and liabilities would increase or decrease by \$4,424,000 and \$612,000, respectively, and our net sales and net earnings would increase or decrease by \$3,099,000 and \$289,000, respectively, on an annual basis.

We also maintain intercompany balances and loans receivable with subsidiaries with different local currencies. These amounts are at risk of foreign exchange losses if exchange rates fluctuate. Assuming a hypothetical aggregate change in the exchange rates of foreign currencies against the U.S. dollar of 10% at March 4, 2006, our pre-tax earnings would be favorably or unfavorably impacted by approximately \$716,000 on an annual basis.

## Interest Rate Risk

Our excess cash is invested in highly liquid, short-term, investment grade securities with maturities of less than one year. These investments are not held for speculative or trading purposes. Changes in interest rates may affect the investment income we earn on cash, cash equivalents and debt

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securities and therefore affect our cash flows and results of operations. As of March 4, 2006, we were exposed to interest rate change market risk with respect to our investments in tax-free municipal bonds in the amount of \$26,660,000. The bonds bear interest at a floating rate established between seven and 35 days. For the nine months ended March 4, 2006, the after-tax interest rate on the bonds approximated 2.7%. Each 100 basis point (or 1%) fluctuation in interest rates will increase or decrease interest income on the bonds by approximately \$267,000 on an annual basis.

As our principal amount of fixed interest rate financing approximated \$273,000 at March 4, 2006, a change in interest rates would not materially impact results of operations or financial position. At March 4, 2006, we did not maintain any variable interest rate financing.

As of March 4, 2006, we have available \$1,762,000 under a working capital bank line of credit, of which no amounts were outstanding. Advances under this line of credit will bear interest at an annual rate indexed to prime. We will thus be exposed to interest rate risk with respect to this credit facility to the extent that interest rates rise when there are amounts outstanding under this facility.

## Item 4. Controls and Procedures

### Evaluation of Disclosure Controls and Procedures

As required by Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the Exchange Act), we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of March 4, 2006. This evaluation was carried out under the supervision and with participation of our Chief Executive Officer and Chief Financial Officer. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Therefore, effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon our evaluation, our Chief Executive Officer and Chief

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Financial Officer concluded that our disclosure controls and procedures are effective as of March 4, 2006, to provide reasonable assurance that information required to be disclosed in the reports that are filed under the Exchange Act is recorded, processed, summarized and reported in a timely manner and is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

### **Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting during the quarter ended March 4, 2006 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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### **E-Z-EM, Inc. and Subsidiaries**

### **Part II: Other Information**

#### **Item 1. Legal Proceedings**

Certain legal proceedings in which we are involved are discussed in Part I, Item 3 of our Annual Report on Form 10-K for the fiscal year ended May 28, 2005.

#### **Item 1A. Risk Factors**

Not applicable.

Item 2. **Unregistered Sales of Securities and Use of Proceeds**

None.

Item 3. **Defaults Upon Senior Securities**

None.

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

None.

Item 5. **Other Information**

None.

Item 6. **Exhibits**

<b><u>No.</u></b>	<b><u>Description</u></b>	<b><u>Page</u></b>
3.1	Restated Certificate of Incorporation of the Registrant, as Amended	(a)
3.2	Amended and Restated Bylaws of the Registrant	(b)
<u>31.1</u>	<u>Certification pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Anthony A. Lombardo)</u>	<u>40</u>
<u>31.2</u>	<u>Certification pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Dennis J. Curtin)</u>	<u>42</u>
<u>32.1</u>		<u>44</u>



Certification pursuant to Title 18, United States Code, Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Anthony A. Lombardo)

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32.2 Certification pursuant to Title 18, United States Code, Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Dennis J. Curtin)

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(a) Incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form 8-A filed with the Commission

on April 8, 2005.

(b) Incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed with the Commission on

January 21, 2005.

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**SIGNATURES**

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Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

E-Z-EM, Inc.

(Registrant)

Date April 13, 2006

Anthony A. Lombardo, President,

Chief Executive Officer, Director

/s/ Anthony A. Lombardo

Date April 13, 2006

Dennis J. Curtin, Senior Vice

President - Chief Financial Officer (Principal Financial and Chief Accounting Officer)

/s/ Dennis J. Curtin

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