ARVINMERITOR INC
Form 10-K
November 20, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended October 1, 2006

Commission file number 1-15983

ARVINMERITOR, INC.

(Exact name of registrant as specified in its charter)

Indiana **(State or other jurisdiction of incorporation or organization)**	**38-3354643** **(I.R.S. Employer Identification No.)**
2135 West Maple Road **Troy, Michigan** **(Address of principal executive offices)**	**48084-7186** **(Zip Code)**

Registrant s telephone number, including area code: (248) 435-1000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class	**Name of each exchange on which registered**
Common Stock, $1 Par Value (including the associated Preferred Share Purchase Rights)	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [X] No [ ]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes [ ] No [X]

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 [X] No [ ]

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

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

Large accelerated filer [X] 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 [X]

The aggregate market value of the registrant s voting and non-voting common equity held by non-affiliates of the registrant on March 31, 2006 (the last business day of the most recently completed second fiscal quarter) was approximately $1,042.4 million.

70,654,731 shares of the registrant s Common Stock, par value $1 per share, were outstanding on October 31, 2006.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the Proxy Statement for the Annual Meeting of Shareowners of the registrant to be held on January 26, 2007 is incorporated by reference into Part III.

PART I

Item 1. ***Business*.**

ArvinMeritor, Inc. (the "company" or "ArvinMeritor"), headquartered in Troy, Michigan, is a global supplier of a broad range of integrated systems, modules and components serving light vehicle, commercial truck, trailer and specialty original equipment manufacturers and certain aftermarkets.

ArvinMeritor was incorporated in Indiana in 2000 in connection with the merger of Meritor Automotive, Inc. ("Meritor") and Arvin Industries, Inc. ("Arvin"). As used in this Annual Report on Form 10-K, the terms "company," "ArvinMeritor," "we," "us" and "our" include ArvinMeritor, its consolidated subsidiaries and its predecessors unless the context indicates otherwise.

The company s fiscal quarters end on the Sundays nearest December 31, March 31 and June 30, and its fiscal year ends on the Sunday nearest September 30. Fiscal year 2006 ended on October 1, 2006 and fiscal year 2005 ended on October 2, 2005. All year and quarter references relate to our fiscal year and fiscal quarters unless otherwise stated. For ease of presentation, September 30 is utilized consistently throughout this report to represent the fiscal year end.

Whenever an item of this Annual Report on Form 10-K refers to information in the Proxy Statement for the Annual Meeting of Shareowners of ArvinMeritor to be held on January 26, 2007 (the "2007 Proxy Statement"), or under specific captions in Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations* or Item 8. *Financial Statements and Supplementary Data,* the information is incorporated in that item by reference.

ArvinMeritor serves a broad range of original equipment manufacturer ("OEM") customers worldwide, including truck OEMs, light vehicle OEMs, trailer producers and specialty vehicle manufacturers, and certain aftermarkets. Our total sales from continuing operations in fiscal year 2006 were $9.2 billion. Our ten largest customers accounted for approximately 74% of fiscal year 2006 sales from continuing operations. We operated 112 manufacturing facilities in 26 countries around the world in fiscal year 2006, including facilities operated by discontinued operations and joint ventures in which we have interests. Sales from continuing operations outside North America accounted for approximately 50% of total sales from continuing operations in fiscal year 2006. Our continuing operations also participated in ten significant non-consolidated joint ventures that generated revenues of approximately $1.8 billion in fiscal year 2006.

In fiscal year 2006, we served customers worldwide through the following businesses:

Continuing Operations:

- Light Vehicle Systems ("LVS") supplies emissions systems, aperture systems (roof and door systems), and undercarriage systems (suspension systems and modules and wheel products) for passenger cars, all-terrain vehicles, light trucks and sport utility vehicles to OEMs.
- Commercial Vehicle Systems ("CVS") supplies drivetrain systems and components, including axles and drivelines, braking systems, suspension systems, and exhaust and ride control products for medium- and heavy-duty trucks, trailers and specialty vehicles to OEMs and to the commercial vehicle aftermarket.

Discontinued Operations:

Light Vehicle Aftermarket ("LVA") supplied exhaust, ride control, motion control and filter products and other automotive parts to the passenger car, light truck and sport utility aftermarket. In October 2004, we announced our intention to divest our LVA business, and we reported this business in discontinued operations for accounting purposes. A significant portion of the LVA businesses were sold in fiscal year 2006, and we expect to complete the divestiture of the remaining LVA businesses in fiscal year 2007. See Strategic Initiatives below.

LVS provided ride control products, including shock absorbers, struts, ministruts and corner modules to OEMs. We substantially completed our plan to exit this business in the first quarter of fiscal year 2006, and we sold the assets related to our shock rod and shock assembly business in the fourth quarter of fiscal year 2006. This business is reported in discontinued operations.

See Notes 1 and 4 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below for information with respect to changes in continuing and discontinued operations and a write-off associated with impairment of goodwill in fiscal year 2006.

See Item 1A. *Risk Factors* below for information on certain risks that could have an impact on our business, financial condition or results of operations in the future.

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Note 24 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* contains financial information by segment for continuing operations for each of the three years ended September 30, 2006, including information on sales and assets by geographic area. The heading "Products" below includes information on LVS and CVS sales by product for each of the three fiscal years ended September 30, 2006.

References in this Annual Report on Form 10-K to our being a leading supplier or the world's leading supplier, and other similar statements as to our relative market position are based principally on calculations we have made. These calculations are based on information we have collected, including company and industry sales data obtained from internal and available external sources, as well as our estimates. In addition to such quantitative data, our statements are based on other competitive factors such as our technological capabilities, our research and development efforts and innovations and the quality of our products and services, in each case relative to that of our competitors in the markets we address.

Business Strategies

We are a global supplier of a broad range of integrated systems, modules and components for use in commercial, specialty and light vehicles worldwide and we have developed market positions as a leader in most of our served markets. We are working to enhance our leadership positions and capitalize on our existing customer, product and geographic strengths, and to increase sales, earnings and profitability. To achieve these goals, we are working to: (a) rationalize our operations by eliminating excess capacity, (b) refocus our business by evaluating our product portfolio to identify our core competencies, and (c) regenerate and grow the businesses that offer attractive returns. In addition, in November 2006 we announced a new profit improvement initiative, Performance Plus, designed to improve cash flow, earnings and shareowner value.

Several significant factors and trends in the automotive industry present opportunities and challenges to industry suppliers and influence our business strategies. These factors and trends include the cyclicality of the industry; consolidation and globalization of OEMs and their suppliers; increased outsourcing by OEMs; increased demand for modules and systems by OEMs; pricing pressures from OEMs that could negatively impact suppliers earnings even when sales volumes are increasing; the rising cost of raw materials, primarily steel and oil; and an increasing emphasis on engineering and technology. Our specific business strategies, described below, are influenced by these industry factors and trends and are focused on leveraging our resources to create a competitive cost structure.

Minimize the Risks of Cyclicality Through Business Diversity. The automotive industry is cyclical in nature and subject to periodic fluctuations in demand for vehicles. This in turn results in fluctuations in demand for our products. We seek to diversify our business in order to mitigate the effects of market downturns and better accommodate the changing needs of OEMs. We strive to maintain diversity in three areas:

Products. We manufacture and sell a wide range of products in various segments of the automotive and commercial vehicle market. For fiscal year 2006, our annual sales from continuing operations include $4.9 billion for LVS and $4.3 billion for CVS.

Customers. A diverse customer base helps to mitigate market fluctuations. We have a large customer base comprised of most major vehicle producers.

Global Presence. Cycles in the major geographic markets of the automotive industry are not necessarily concurrent or related. We seek to maintain a strong global presence and to expand our global operations to mitigate the effect of periodic fluctuations in demand in one or more geographic areas. A strong global presence also helps to meet the global sourcing needs of our customers.

Focus on Organic Growth While Reviewing Strategic Opportunities. Our goal is to grow businesses that offer attractive returns and are core to our operations. We have identified the areas of our core business that we believe have the most potential for leveraging into other products and

markets, and we are focusing our resources on these areas. We also seek to take advantage of opportunities for operating synergies and cross-selling of products between our light vehicle and commercial vehicle businesses. For example, we continue to adapt products and technologies, originally developed by the LVS emissions technologies business unit, in the development of emissions control products for its commercial vehicle customers. See Products Commercial Vehicle Systems Undercarriage and Drivetrain Systems Emissions Systems below. In addition, we are exploring opportunities to apply our CVS drivetrain expertise in the development of undercarriage component systems for our LVS customers.

We also consider strategic opportunities that could enhance the company s growth. Automotive suppliers continue to consolidate into larger, more efficient and more capable companies and collaborate with each other in an effort to better serve the global needs of their OEM customers. We regularly evaluate various strategic and business development opportunities, including licensing agreements, marketing arrangements, joint ventures, acquisitions and dispositions. We remain committed to selectively pursuing alliances and acquisitions that would allow us to leverage our capabilities, gain access to new customers and technologies, enter new product markets and implement our business strategies. We also continue to review the prospects of our existing businesses to determine whether any of them should be modified, restructured, sold or otherwise discontinued. See Strategic Initiatives and Joint Ventures below for information on recent activities in these areas.

Grow Content Per Vehicle Through Technologically Advanced Systems and Modules. Increased outsourcing by OEMs has resulted in higher overall per vehicle sales by independent suppliers. This presents an opportunity for supplier sales growth at a faster rate than the overall automotive industry growth trend. OEMs are also demanding modules and integrated systems that require little assembly by the OEM customer.

One of our significant growth strategies is to provide engineering and design expertise, develop new products and improve existing products that meet these customer needs. We will continue to invest in new technologies and product development and work closely with our customers to develop and implement design, engineering, manufacturing and quality improvements. We will also continue to integrate our existing product lines by using our design, engineering and manufacturing expertise and teaming with technology partners to expand sales of higher-value modules and systems.

Management believes that the strategy of continuing to introduce new and improved systems and technologies will be an important factor in our efforts to achieve our growth objectives. We will draw upon the engineering resources of our technical centers in Detroit, Michigan; Columbus, Indiana; and Augsburg, Germany, and our engineering centers of expertise in the United States, Brazil, Canada, France, Germany, India and the United Kingdom. See Research and Development below.

Enhance Core Products to Address Safety and Environmental Issues. Another industry trend is the increasing amount of equipment required for changes in environmental and safety-related regulatory provisions. OEMs select suppliers based not only on the cost and quality of products, but also on their ability to meet these demands. We use our technological expertise to anticipate trends and to develop products that address safety and environmental concerns.

To address safety, our LVS group designs its aperture systems with stronger materials, creates designs that enhance the vehicle s crashworthiness and develops undercarriage systems that offer improved ride and vehicle control dynamics. Our CVS group is focusing on the integration of braking and stability products and suspension products, as well as the development of electronic control capabilities. CVS, through its Meritor WABCO joint venture, is also developing braking systems technology to improve braking performance and reduce stopping distances for commercial motor vehicles.

With respect to emissions regulations, LVS is an industry leader in emissions technologies that improve fuel economy and reduce air pollutants, while we are leveraging our expertise in light vehicle emissions technologies to bring products to the commercial vehicle market. Looking forward, we will continue to seek to develop products that will permit us to assist customers in meeting new and more stringent emissions requirements that will be phased in over the next several years in our North American, European and Asia/Pacific markets.

We believe these more stringent emissions regulations will result in continued growth in Europe, and potential growth in North America, of diesel engines. Diesel engines today have the advantage of improved fuel economy, better performance and improving emissions levels. LVS began production in 2004 under contracts to provide diesel emissions systems to light vehicle OEMs in Europe. In fiscal year 2006, approximately 47% of all new vehicles in Europe were sold with diesel engine powertrains.

Strengthen our Presence in Emerging Global Markets. Geographic expansion to meet the global sourcing needs of customers and to address new markets is an important element of our growth strategy. ArvinMeritor currently has joint ventures and wholly-owned subsidiaries in China and India and participates in programs to support customers as they establish and expand operations in those markets. We also have wholly-owned operations and regional joint ventures in South America, a market with potential for significant growth.

Drive a Continuous Improvement Culture Focused on Return on Capital. The ArvinMeritor Performance System (AMPS) is a continuous improvement initiative that guides our philosophy for achieving operational excellence, eliminating waste, improving quality and earning customer loyalty. Throughout the company, continuous improvement teams work to achieve significant cost savings, increase productivity and efficiency and streamline operations. They focus on eliminating non-value-added tasks, reducing lead and cycle times and improving customer service. A continuous improvement culture is important to our business operations and to maintaining and improving our earnings.

Products

ArvinMeritor designs, develops, manufactures, markets, distributes, sells, services and supports a broad range of products for use in commercial, specialty and light vehicles. In addition to sales of original equipment systems and components, we provide our products to OEMs, dealers, distributors, fleets and other end-users in certain aftermarkets.

In recent years, we have executed a strategy of analyzing our product portfolio and refocusing the business on our core competencies, resulting in divestiture of some businesses and product lines. Since the beginning of fiscal year 2006, we have sold a significant portion of the LVA business and have exited the LVS ride control business (see Strategic Initiatives and Joint Ventures below). All of these businesses have been reported in discontinued operations for accounting purposes.

The following chart sets forth operating segment sales as a percentage of total sales for continuing operations by product for each of the three fiscal years ended September 30, 2006. A narrative description of the principal products of our continuing operations, as well as the principal products of our discontinued operations, follows the chart.

	Fiscal Year Ended September 30,		
LVS:	**2006**	**2005**	**2004**
Emissions Technologies	31 %	29 %	33 %
Aperture Systems	13 %	15 %	19 %
Undercarriage Systems	9 %	10 %	7 %
Total LVS	53 %	54 %	59 %
CVS:			
Undercarriage and Drivetrain Systems	43 %	40 %	35 %
Specialty Systems (1)	4 %	6 %	6 %
Total CVS	47 %	46 %	41 %
Total	100 %	100 %	100 %

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(1) In October 2005, we sold certain assets of our off-highway brake business (see Strategic Initiatives below). Sales from these products are included in CVS Specialty Systems for fiscal years 2004 and 2005.

Light Vehicle Systems

Emissions Technologies

We are a leading global supplier of a complete line of exhaust systems and exhaust system components, including mufflers, exhaust pipes, catalytic converters, diesel particulate filters and exhaust manifolds. We sell these products to OEMs primarily as original equipment, while also supporting manufacturers needs for replacement parts and dealers needs for service parts. We participate in this business both directly and through joint ventures and affiliates. These alliances include our 50% interest in Arvin Sango Inc., an exhaust joint venture based in North America.

See Business Strategies Enhance Core Products to Address Safety and Environmental Issues above for information on the importance of diesel technology to LVS strategies for future growth.

Aperture Systems

Roof Systems. ArvinMeritor is one of the world's leading independent suppliers of sunroofs and roof systems products for use in passenger cars, light trucks and sport utility vehicles, including our Golde® brand sunroofs. We make complete roofs, some of which incorporate sunroofs, that provide OEMs with cost savings by reducing assembly time and parts. Our roof system manufacturing facilities are located in North America and Europe.

Door Systems. We are a leading supplier of integrated door modules and systems, including manual and power window regulators and latch systems. Our power and manual door system products utilize numerous technologies, including our own electric motors with electronic function capabilities, including anti-squeeze technologies, which are custom designed for individual applications to maximize operating efficiency and reduce noise levels. We manufacture window regulators at plants in North and South America, Europe and the Asia/Pacific region for light vehicle and heavy-duty commercial vehicle OEMs.

We also supply manual and power activated latch systems to light vehicle manufacturers. Our access control products include modular and integrated door latches, actuators, trunk and hood latches and fuel flap locking devices, with a leadership market position in Europe. We manufacture access control systems at assembly facilities in North and South America, Europe and the Asia/Pacific region.

Undercarriage Systems

Suspension Systems. We are one of the leading independent suppliers of products used in suspension systems for passenger cars, light trucks and sport utility vehicles in North America through our 57%-owned joint venture with Mitsubishi Steel Manufacturing Co. Our suspension system products, which are manufactured at facilities in the United States and Canada, include coil springs, stabilizer bars and torsion bars.

Suspension Modules. Using our expertise in ride control and vehicle dynamics, we offer final assembly of upper and complete corner modules as well as front and rear cross vehicle modules. This capability gives us the ability to incorporate components that we manufacture into these modules, thus enhancing value content.

Wheel Products. We are a leading supplier of steel wheel products to the light vehicle OEM market, principally in North and South America. We have wheel manufacturing facilities in Brazil and Mexico. Our wheel products include fabricated steel wheels, bead seat attached wheels, full-face designed wheels and clad wheels with the appearance of a chrome finish. Our cladding process offers enhanced styling options previously available only in aluminum wheels.

Commercial Vehicle Systems

Undercarriage and Drivetrain Systems

Truck Axles. We are one of the world's leading independent suppliers of axles for medium- and heavy-duty commercial vehicles, with axle manufacturing facilities located in North America, South America, Europe and the Asia/Pacific region. Our extensive truck axle product line includes a wide range of drive and non-drive front steer axles and single and tandem rear drive axles, which can include driver-controlled differential lock for extra traction, aluminum carriers to reduce weight and pressurized filtered lubrication systems for longer life. Our front steer and rear drive axles can be equipped with our cam, wedge or disc brakes, automatic slack adjusters and anti-lock braking systems.

Drivelines and Other Products. We also supply universal joints and driveline components, including our Permalube universal joint and Permalube driveline, which are low maintenance, permanently lubricated designs used in the high mileage on-highway market.

Suspension Systems and Trailer Products. We are one of the world's leading manufacturers of heavy-duty trailer axles, with leadership positions in North America and in Europe. Our trailer axles are available in over 40 models in capacities from 20,000 to 30,000 pounds for virtually all heavy trailer applications and are available with our broad range of brake products, including anti-lock braking systems (ABS). In addition, we supply trailer air suspension systems and products for which we have strong market positions in Europe and an increasing market presence in North America.

Through our 50%-owned joint venture with Randon Participacoes, we develop, manufacture and sell truck suspensions, trailer axles and suspensions and related wheel-end products in the South American market.

In the fourth quarter of fiscal year 2006, we announced our intention to build a new trailer axle and suspension system facility in China, to supply OEMs in the Chinese market and to export components to the North American and European markets. The facility is scheduled to begin production in the first half of 2007.

Braking Systems. We are a leading independent supplier of air and hydraulic brakes to medium- and heavy-duty commercial vehicle manufacturers in North America and Europe. In Brazil, the third largest truck and trailer market in the world, our 49%-owned joint venture with Randon S. A. Veiculos e Implementos is a leading supplier of brakes and brake-related products.

Through manufacturing facilities located in North America and Europe, we manufacture a broad range of foundation air brakes, as well as automatic slack adjusters for brake systems. Our foundation air brake products include cam drum brakes, which offer improved lining life and tractor/trailer interchangeability; air disc brakes, which provide fade resistant braking for demanding applications; wedge drum brakes, which are lightweight and provide automatic internal wear adjustment; hydraulic brakes; and wheel end components such as hubs, drums and rotors.

Federal regulations require that new heavy- and medium-duty vehicles sold in the United States be equipped with ABS. Our 50%-owned joint venture with WABCO Automotive Products ("WABCO"), a wholly-owned subsidiary of American Standard Inc., is the leading supplier of ABS and a supplier of other electronic and pneumatic control systems for North American heavy-duty commercial vehicles. The joint venture also supplies hydraulic ABS to the North American medium-duty truck market and produces stability control systems for tractors and trailers, which are designed to help maintain vehicle stability and aid in reducing tractor-trailer rollovers.

Transmissions. In fiscal year 2004, we dissolved our 50%-owned joint venture with ZF Friedrichshafen AG ("ZF), which produced transmission components and systems for heavy vehicle OEMs and the aftermarket in the United States, Canada and Mexico. The joint venture was replaced by a marketing arrangement that allows us to provide the redesigned FreedomLine , a fully automated mechanical truck transmission without a clutch pedal, to our customers. This transmission product line enabled us in fiscal year 2006 to supply a complete drivetrain system to heavy-duty commercial vehicle manufacturers in North America.

Emissions Systems. CVS has adapted products and applications from the LVS emissions technologies business unit and introduced new technologies to develop a portfolio of technologically advanced emissions control products and applications to address increasingly stringent regulatory standards for diesel particulate matter and nitrogen oxide (NOx) emissions in commercial vehicles. These products and applications include:

Diesel Oxidation Catalysts capable of removing up to 90% of hydrocarbon and carbon monoxide emissions and 30% of particulate matter. This technology is available currently.
Thermal Regenerator on demand, active regeneration technology that offers a safe and effective way to remove diesel particulate matter, using diesel fuel as a heat source, without the use of a catalytic coating or precious metals. This technology was released for OEM use in 2006, in preparation for the EPA s 2007 particulate matter emission standards.
Catalyzed Diesel Particulate Filter a filter that traps the diesel particulate matter from the exhaust and prevents it from reaching the atmosphere. It is expected to be available in 2007 to meet the new 2007 U.S. regulations.
Selective Catalytic Reduction (SCR) System a compact, low-weight option to effectively reduce NOx emissions to the levels required to meet 2008 European standards. The system also achieves reduction of diesel particulate matter and allows the engine to operate in ways that could maximize fuel economy.
Plasma Fuel Reformer a system that creates a hydrogen-rich gas from hydrocarbon fuel sources, which enables more efficient control of NOx from diesel engine exhaust through effective regeneration of NOx adsorbers or lean NOx traps. This technology could be less sensitive to sulfur contamination and could use less fuel than conventional regeneration and consume minimal power. This technology, which is expected to be available for production in 2010, also has potential for future applications in gasoline combustion engines.

Specialty Systems

Off-Highway Vehicle Products. We supply heavy-duty axles and drivelines in the Asia/Pacific region, for use in numerous off-highway vehicle applications, including construction, material handling, agriculture, mining and forestry. These products are designed to tolerate high tonnages and operate under extreme conditions. Prior to the first quarter of fiscal year 2006, when we sold the off-highway brakes business (see Strategic Initiatives below), we also supplied brakes in North America, South America, Europe and the Asia/Pacific region.

Government Products. We supply axles, brakes and brake system components including ABS, trailer products, transfer cases and drivelines for use in medium-duty and heavy-duty military tactical wheeled vehicles, principally in North America.

Specialty Vehicle Products. We supply axles, brakes and transfer cases for use in buses, coaches and recreational, fire and other specialty vehicles in North America and Europe, and we are the leading supplier of bus and coach axles and brakes in North America.

Discontinued Operations

Light Vehicle Aftermarket. Prior to the divestiture of a significant portion of the LVA businesses in fiscal year 2006 (see Strategic Initiatives), the principal LVA products included mufflers; exhaust and tail pipes; catalytic converters; shock absorbers; struts; gas lift supports and vacuum actuators; and automotive oil, air, and fuel filters. These products were sold under the brand names Arvin® (mufflers); Gabriel® (shock absorbers); and Purolator® (filters). LVA also marketed products under private label to some customers.

LVS Ride Control Systems. Prior to exiting this business in fiscal year 2006 (see Strategic Initiatives below), we provided ride control products, including shock absorbers, struts, ministruts and corner modules to OEMs.

Customers; Sales and Marketing

ArvinMeritor's operating segments have numerous customers worldwide and have developed long-standing business relationships with many of these customers. Our ten largest customers accounted for approximately 74% of our total sales from continuing operations in fiscal year 2006. In recent years, we have been adversely impacted by the weakened financial strength of certain of our customers, including those that have filed for protection under bankruptcy and administration laws. See Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations Overview* and *Results of Operations.*

Both LVS and CVS market and sell products principally to OEMs. LVS and CVS generally compete for new business from OEMs, both at the beginning of the development of new vehicle platforms and upon the redesign of existing platforms. New platform development generally begins two to four years prior to start-up of production. In North America, CVS also markets truck and trailer products directly to dealers, fleets and other end-users, which may designate the components and systems of a particular supplier for installation in the vehicles they purchase from OEMs. CVS also provides truck and trailer products and off-highway and specialty products to OEMs, dealers and distributors in the aftermarket.

Consistent with industry practice, LVS and CVS make most of their sales to OEMs through open purchase orders, which do not require the purchase of a minimum number of products. The customer typically may cancel these purchase orders on reasonable notice. LVS and CVS also sell products to certain customers under long-term arrangements that require us to provide annual cost reductions (through price reductions or other cost benefits for the OEMs). If we are unable to generate sufficient cost savings in the future to offset such price reductions, our gross margins will be adversely affected (see Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations* below).

See Item 1A. *Risk Factors* for information on customers accounting for 10% or more of our consolidated revenues in fiscal year 2006 and certain risks associated with our dependence on large OEM customers.

Competition

LVS and CVS compete worldwide with a number of North American and international providers of components and systems, some of which are owned by or associated with some of our customers. The principal competitive factors are price, quality, service, product performance, design and engineering capabilities, new product innovation and timely delivery. In addition, certain OEMs manufacture for their own use products of the types we supply.

LVS has numerous competitors across its various product lines worldwide, including Tenneco, Faurecia, Eberspaecher and Benteler (emissions technologies); Webasto, Inalfa and Aisin (roof systems); Brose, Intier, Kiekert AG, Mitsui, Valeo, Aisin and Grupo Antolin (door and access control systems); Tenneco Automotive, ZF, Delphi, Thyssen-Krupp, Benteler and TRW (suspension modules); Thyssen-Krupp, NHK Spring, Rassini, Mubea and Sogefi (suspension systems); and Hayes-Lemmerz, Topy, Accuride and CMW (wheel products). The major competitors of CVS are Dana Corporation (truck axles and drivelines); Knorr/Bremse, Haldex and WABCO (braking systems); Hendrickson and Neway (suspension systems); Hendrickson and Dana (trailer products); and Eaton Corporation (transmissions).

See Item 1A. *Risk Factors* for information on certain risks associated with our competitive environment.

Raw Materials and Supplies

We concentrate our purchases of certain raw materials and parts over a limited number of suppliers, some of which are located in developing countries and some of which are in weakened financial condition. We are dependent upon the ability of our suppliers to meet performance and quality specifications and delivery schedules. The inability of a supplier to meet these requirements, the loss of a significant supplier, or any labor issues or work stoppages at a significant supplier, could have an adverse effect on us.

Prices of certain raw materials, primarily steel and oil, for our business segments' manufacturing needs negatively impacted our operating income in fiscal year 2006. We are taking actions to mitigate the effects of higher steel prices, including alternative sourcing of materials or components, consolidating and selling scrap from our facilities, re-engineering our products to be less dependent on steel, and negotiating with customers to recover some of the increased costs, and we have had some success in recovering a portion of higher steel prices from our customers. However, if supplies are inadequate for our needs, or if prices remain at current levels or increase and we are unable to either pass these prices to our customer base or otherwise mitigate the costs, our operating income could continue to be adversely affected.

Strategic Initiatives

As described above, our business strategies are focused on enhancing our market position by eliminating excess capacity, evaluating our product portfolio to identify our core competencies, and growing the businesses that offer the most attractive returns. Implementing these strategies involves various types of strategic initiatives.

Restructuring. As part of our strategy to rationalize our business, in fiscal year 2005, we announced restructuring plans with respect to continuing operations to eliminate approximately 500 salaried positions and 1,750 hourly positions and to consolidate, downsize, close or sell 11 global facilities, primarily in the LVS segment. During fiscal year 2006, we identified approximately 550 salaried and hourly additional headcount reductions in LVS. These actions are intended to align capacity with industry conditions, utilize assets more efficiently and improve operations. Estimated total costs of $135 million include employee severance and other exit costs, as well as asset impairments. Total costs recorded for these actions are $127 million, of which $37 million was recorded in fiscal year 2006. We expect to complete these restructuring actions and record the remaining costs in fiscal year 2007. See Note 5 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below.

In addition, we recently announced plans to restructure our emissions technologies business in response to significant challenges, including higher raw material costs, intense pricing pressures, increased competition and a downturn in production at certain North American manufacturers. These plans include downsizing certain facilities and realigning our manufacturing footprint to utilize assets more efficiently, improve operations and lower costs. The total estimated cost of these actions is $50 million, of which approximately $40 million is expected to be cash costs. This restructuring program will be executed over the next 12 to 36 months. No amounts have been recorded for this restructuring program at September 30, 2006.

Divestitures. As part of our strategy to refocus our business, we regularly review the prospects of our existing businesses to determine whether any of them should be modified, restructured, sold or otherwise discontinued. We completed the following initiatives since the beginning of fiscal year 2006 (see Notes 3 and 6 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below):

- We previously announced our intention to divest the LVA business segment, enabling the company to focus more resources on our core competencies and thereby better support our OEM customers. Since the beginning of fiscal year 2006, a significant portion of the LVA businesses have been sold, including the following transactions. We expect to complete the divestiture of the remaining LVA businesses in fiscal year 2007.
  - We sold our 39% interest in Purolator India, a joint venture, in the first quarter of fiscal year 2006;
  - We completed the sale of our LVA North American filters and exhaust businesses in the second quarter of fiscal year 2006; and
  - We completed the sale of our Gabriel South Africa ride control business and our North American motion control business in the fourth quarter of fiscal year 2006.
- In the first quarter of fiscal year 2006, we sold certain assets of our CVS off-highway brakes business.
- In the first quarter of fiscal year 2006, we sold our LVS ride control business located in Asti, Italy, and in the fourth quarter of fiscal year 2006, we completed the sale of the assets related to our shock rods and shock assemblies business. These sales, together with previous divestitures, complete our plan to exit the LVS ride control business.

Acquisitions and Other Growth Initiatives. As part of our strategy to regenerate our profitable businesses, we regularly consider various strategic and business opportunities, including licensing agreements, marketing arrangements and acquisitions, as well as joint ventures (discussed

below). We believe that the industry in which we operate could experience significant further consolidation among suppliers. This trend is due in part to globalization and increased outsourcing of product engineering and manufacturing by OEMs, and in part to OEMs reducing the total number of their suppliers by more frequently awarding long-term, sole-source or preferred supplier contracts to the most capable global suppliers. Speed is an important competitive factor, with the fastest industry participants able to maximize key resources and contain costs.

No assurance can be given as to whether or when any strategic growth initiatives will be consummated in the future. We will continue to consider acquisitions as a means of growing the company or adding needed technologies, but cannot predict whether our participation or lack of participation in industry consolidation will ultimately be beneficial to us.

See Item 1A. *Risk Factors* for information on certain risks associated with strategic initiatives.

Joint Ventures

As the automotive industry has become more globalized, joint ventures and other cooperative arrangements have become an important element of our business strategies. As of September 30, 2006, our continuing operations participated in 26 joint ventures with interests in the United States, Brazil, Canada, China, Colombia, the Czech Republic, France, Germany, India, Italy, Korea, Mexico, the Slovak Republic, Turkey, the United Kingdom and Venezuela.

In accordance with accounting principles generally accepted in the United States, our consolidated financial statements include the operating results of those majority-owned joint ventures in which we have control. Significant unconsolidated joint ventures include our 50%-owned North American joint venture with WABCO (ABS systems for heavy-duty commercial vehicles) and our 50% interest in Arvin Sango Inc. (emissions technologies) in the United States (see Note 13 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below).

Since the beginning of fiscal year 2006, we completed the following significant initiatives with respect to our joint ventures:

As noted above, in the first quarter of fiscal year 2006, we sold our 39% interest in the Purolator India LVA joint venture.

In the fourth quarter of fiscal year 2006, LVS formed a joint venture with Pyeong Hwa automotive for the final assembly of fully integrated door modules for Kia Motors Corporation s new facility in Slovakia.

Research and Development

We have significant research, development, engineering and product design capabilities. We spent $177 million in fiscal year 2006, $171 million in fiscal year 2005 and $157 million in fiscal year 2004 on company-sponsored research, development and engineering. At September 30, 2006, we employed approximately 1,450 professional engineers and scientists.

Patents and Trademarks

We own or license many United States and foreign patents and patent applications in our manufacturing operations and other activities. While in the aggregate these patents and licenses are considered important to the operation of our businesses, management does not consider them of such importance that the loss or termination of any one of them would materially affect a business segment or ArvinMeritor as a whole.

Our registered trademarks ArvinMeritor®, Arvin® and Meritor® are important to our business. Other significant trademarks owned by us include Fumagalli (wheels), Zeuna Stärker® (emissions systems) and Golde® (sunroofs) with respect to LVS; and ROR (trailer axles) with respect to CVS. In connection with the 1997 spin-off of Meritor s common stock to the shareowners of Rockwell International Corporation (now Rockwell Automation, Inc., and referred to in this Annual Report on Form 10-K as Rockwell) and the transfer of Rockwell s automotive businesses to Meritor, Meritor entered into an agreement that allows us to continue to apply the "Rockwell" brand name to our products until September 30, 2007.

Substantially all of our intellectual property is subject to a first priority perfected security interest securing our obligations to the lenders under our credit facility. See Note 16 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below.

Employees

At September 30, 2006, we had approximately 27,500 full-time employees. At that date, approximately 4,100 employees in the United States and Canada were covered by collective bargaining agreements and most of our facilities outside of the United States and Canada were unionized. We believe our relationship with unionized employees is satisfactory.

Our collective bargaining agreement with the Canadian Auto Workers (CAW) at our CVS brakes facility in Ontario, Canada, expired on June 3, 2006. On June 4, 2006, we announced that, after lengthy negotiations, a new tentative agreement with the CAW had not yet been reached and, as a result, we had suspended operations at the facility. On June 12, 2006, we reached a tentative agreement with the CAW, which was subsequently ratified on June 14, 2006, and resumed operations. As a result of this work stoppage, we experienced temporary manufacturing inefficiencies and incurred certain costs in order to return to normal production. See Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations- Overview* and Note 23 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below for information on the estimated financial impact of this work stoppage. Other than the foregoing, no significant work stoppages have occurred in the past five years.

Environmental Matters

Federal, state and local requirements relating to the discharge of substances into the environment, the disposal of hazardous wastes and other activities affecting the environment have, and will continue to have, an impact on our manufacturing operations. We record liabilities for environmental issues in the accounting period in which our responsibility and remediation plan are established and the cost can be reasonably estimated. At environmental sites in which more than one potentially responsible party has been identified, we record a liability for our allocable share of costs related to our involvement with the site, as well as an allocable share of costs related to insolvent parties or unidentified shares. At environmental sites in which we are the only potentially responsible party, we record a liability for the total estimated costs of remediation before consideration of recovery from insurers or other third parties.

We have been designated as a potentially responsible party at seven Superfund sites, excluding sites as to which our records disclose no involvement or as to which our potential liability has been finally determined. In addition to Superfund sites, various other lawsuits, claims and proceedings have been asserted against us, alleging violations of federal, state and local environmental protection requirements or seeking remediation of alleged environmental impairments, principally at previously disposed-of properties. We have established reserves for these liabilities. See Note 23 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below for information as to our estimates of the total reasonably possible costs we could incur and the amounts recorded as a liability as of September 30, 2006, and as to changes in environmental accruals during fiscal year 2006.

The process of estimating environmental liabilities is complex and dependent on physical and scientific data at the site, uncertainties as to remedies and technologies to be used, and the outcome of discussions with regulatory agencies. The actual amount of costs or damages for which we may be held responsible could materially exceed our current estimates because of uncertainties, including the financial condition of other potentially responsible parties, the success of the remediation and other factors that make it difficult to predict actual costs accurately. However, based on management's assessment, after consulting with Vernon G. Baker, II, Esq., General Counsel of ArvinMeritor, and with outside advisors who specialize in environmental matters, and subject to the difficulties inherent in estimating these future costs, we believe that our expenditures for environmental capital investment and remediation necessary to comply with present regulations governing environmental protection and other expenditures for the resolution of environmental claims will not have a material adverse effect on our business, financial condition or results of operations. In addition, in future periods, new laws and regulations, changes in remediation plans, advances in technology and additional information about the ultimate clean-up remedy could significantly change our estimates. Management cannot assess the possible effect of compliance with future requirements.

International Operations

Approximately 48% of our total assets related to continuing operations as of September 30, 2006 and 50% of fiscal year 2006 sales from continuing operations were outside North America. See Note 24 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* below for financial information by geographic area for the three fiscal years ended September 30, 2006. Our international operations are subject to a number of risks inherent in operating abroad (see Item 1A. *Risk Factors* below). There can be no assurance that these risks will not have a material adverse impact on our ability to increase or maintain our foreign sales or on our financial condition or results of operations.

Our operations are also exposed to global market risks, including foreign currency exchange rate risk related to our transactions denominated in currencies other than the U.S. dollar. We have implemented a foreign currency cash flow hedging program to help reduce the company s exposure to changes in exchange rates. We use foreign currency forward contracts to manage the company s exposures arising from foreign currency exchange risk. Gains and losses on the underlying foreign currency exposures are partially offset with gains and losses on the foreign exchange forward contracts. The contracts generally mature within 12 months. It is our policy not to enter into derivative financial instruments for speculative purposes and, therefore, we hold no derivative instruments for trading purposes. See Item 7A. *Quantitative and Qualitative Disclosures About Market Risk* and Note 17 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and*

Supplementary Data below.

Seasonality; Cyclicality

LVS and CVS may experience seasonal variations in the demand for products to the extent automotive vehicle production fluctuates. Historically, for both segments, demand has been somewhat lower in the quarters ended September 30 and December 31, when OEM plants may close during model changeovers and vacation and holiday periods.

In addition, the industries in which LVS and CVS operate have been characterized historically by periodic fluctuations in overall demand for trucks, passenger cars and other vehicles for which we supply products, resulting in corresponding fluctuations in demand for our products. Production and sales of the vehicles for which we supply products generally depend on economic conditions and a variety of other factors that are outside our control, including customer spending and preferences, labor relations and regulatory requirements. See Item 1A. *Risk Factors* below. Cycles in the major automotive industry markets of North America

and Europe are not necessarily concurrent or related. We have sought and will continue to seek to expand our operations globally to mitigate the effect of periodic fluctuations in demand of the automotive industry in one or more particular countries.

The following table sets forth vehicle production in principal markets served by LVS and CVS for the last five fiscal years:

	Year Ended September 30,				
	2006	**2005**	**2004**	**2003**	**2002**
Light Vehicles (in millions):					
North America	15.7	15.6	15.9	15.9	16.3
South America	3.0	2.7	2.3	2.3	1.9
Western Europe (including Czech Republic)	16.4	16.4	16.9	16.9	16.5
Asia/Pacific	24.8	22.5	20.9	20.9	17.3
Commercial Vehicles (in thousands):					
North America, Heavy-Duty Trucks	352	324	235	235	169
North America, Medium-Duty Trucks	216	208	172	172	133
United States and Canada, Trailers	312	327	284	284	145
Western Europe, Heavy- and Medium-Duty Trucks	439	421	376	376	363
Western Europe, Trailers	118	115	109	109	101

Source: Automotive industry publications and management estimates.

We anticipate the North American heavy-duty truck market to decrease approximately 33% in fiscal year 2007, with production at an estimated 235,000 units. In Western Europe, we expect production of heavy- and medium-duty trucks to be approximately 419,000 units. Our most recent outlook shows North American and Western European light vehicle production during fiscal year 2007 to be about the same as fiscal year 2006. See Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations Overview* and *Results of Operations* below for information on the effects of recent market cycles on our sales and earnings.

Available Information

We make available free of charge through our web site (www.arvinmeritor.com) our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, all amendments to those reports, and other filings with the Securities and Exchange Commission (SEC), as soon as reasonably practicable after they are filed.

Cautionary Statement

This Annual Report on Form 10-K contains statements relating to future results of the company (including certain projections and business trends) that are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements are typically identified by words or phrases such as believe, expect, anticipate, estimate, should, are likely to be, will and similar expressic results may differ materially from those projected as a result of certain risks and uncertainties, including but not limited to global economic and market cycles and conditions; the demand for commercial, specialty and light vehicles for which the company supplies products; risks inherent in operating abroad (including foreign currency exchange rates and potential disruption of production and supply due to terrorist attacks or acts of aggression); availability and cost of raw materials, including steel; OEM program delays; demand for and market acceptance of new and existing products; successful development of new products; reliance on major OEM customers; labor relations of the company, its suppliers and customers, including potential disruptions in supply of parts to our facilities or demand for our products due to work stoppages; the financial

condition of the company s suppliers and customers, including potential bankruptcies; possible adverse effects of any future suspension of normal trade credit terms by our suppliers; potential difficulties competing with companies that have avoided their existing contracts in bankruptcy and reorganization proceedings; successful integration of acquired or merged businesses; the ability to achieve the expected annual savings and synergies from past and future business combinations and the ability to achieve the expected benefits of restructuring actions; success and timing of potential divestitures; potential impairment of long-lived assets, including goodwill; competitive product and pricing pressures; the amount of the company s debt; the ability of the company to continue to comply with covenants in its financing agreements; the ability of the company to access capital markets; credit ratings of the company s debt; the outcome of existing and any future legal proceedings, including any litigation with respect to environmental or asbestos-related matters; rising costs of pension and other post-retirement benefits and possible changes in pension and other accounting rules; as well as other risks and uncertainties, including but not limited to those detailed herein and from time to time in other filings of the company with the SEC. See also the following portions of this Annual Report on Form 10-K: Item 1. *Business*, Customers; Sales and Marketing ; Competition ; Raw Materials and

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Supplies ; Strategic Initiatives ; Environmental Matters ; International Operations ; and Seasonality; Cyclicality ; Item 1A. *Risk Factors*; Item 3. *Legal Proceedings*; and Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations*. These forward-looking statements are made only as of the date hereof, and the company undertakes no obligation to update or revise the forward-looking statements, whether as a result of new information, future events or otherwise, except as otherwise required by law.

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

Our business, financial condition and results of operations can be impacted by a number of risks, including those described below and elsewhere in this Annual Report on Form 10-K, any one of which could cause our actual results to vary materially from recent results or from anticipated future results. Any of these individual risks could materially and adversely affect our business, financial condition and results of operations. This effect could be compounded if multiple risks were to occur.

We operate in an industry that is cyclical and that has periodically experienced significant year-to-year fluctuations in demand for vehicles; we also experience seasonal variations in demand for our products.

The industries in which LVS and CVS operate have been characterized historically by periodic fluctuations in overall demand for trucks, passenger cars and other vehicles for which we supply products, resulting in corresponding fluctuations in demand for our products. The cyclical nature of the automotive industry cannot be predicted with certainty.

Production and sales of the vehicles for which we supply products generally depend on economic conditions and a variety of other factors that are outside our control, including customer spending and preferences, labor relations and regulatory requirements. In particular, demand for CVS products can be affected by pre-buy before the effective date of new regulatory requirements, such as changes in emissions standards. Implementation of new, more stringent, emissions standards is scheduled for 2007 and 2010 in the U.S. and 2008 in Europe, and we believe that heavy-duty truck demand in these markets could increase prior to the effective dates of the new regulations, but is likely to fall in North America in 2007 after the new standards are implemented.

LVS and CVS may also experience seasonal variations in the demand for products to the extent that automotive vehicle production fluctuates. Historically, for both segments, demand has been somewhat lower in the quarters ended September 30 and December 31, when OEM plants may close during model changeovers and vacation and holiday periods.

We depend on large OEM customers.

Both LVS and CVS are dependent upon large OEM customers with substantial bargaining power with respect to price and other commercial terms. Loss of all or a substantial portion of sales to any of our large volume customers for whatever reason (including, but not limited to, loss of market share by these customers, loss of contracts, insolvency of such customers, reduced or delayed customer requirements, plant shutdowns, strikes or other work stoppages affecting production by such customers), or continued reduction of prices to these customers, could have a significant adverse effect on our financial results. There can be no assurance that we will not lose all or a portion of sales to our large volume customers, or that we will be able to offset continued reduction of prices to these customers with reductions in our costs.

During fiscal year 2006, DaimlerChrysler AG (which owns Chrysler, Mercedes-Benz AG and Freightliner Corporation), a significant customer of LVS and CVS, accounted for approximately 18% of our total sales from continuing operations. In addition, sales to Volkswagen accounted

for approximately 11% and sales to General Motors Corporation and Ford Motor Company each accounted for approximately 10% of our total sales from continuing operations. No other customer accounted for 10% or more of our total sales from continuing operations in fiscal year 2006. These sales include pass-through components that are acquired and incorporated into our systems or modules at the customer s request.

The level of our sales to large OEM customers depends on their production and sales volumes. Several of our significant customers have major union contracts that expire and are subject to renegotiation over the next few years. Any strikes or other actions that affect our customers production during this process would also affect our sales. Further, to the extent that the financial condition, including bankruptcy, or market share of any of our largest customers deteriorates or their sales otherwise decline, our financial position and results of operations could be adversely affected.

We operate in a highly competitive industry.

Each of ArvinMeritor's businesses operates in a highly competitive environment. LVS and CVS compete worldwide with a number of North American and international providers of components and systems, some of which are owned by or associated with some of our customers. Some of these competitors are larger and have greater financial resources or have established relationships with significant customers. In addition, certain OEMs manufacture for their own use products of the types we supply, and any future increase in this activity could displace LVS and CVS sales.

Many companies in the automotive industry have undertaken substantial contractual obligations to current and former employees, primarily with respect to pensions and other post-retirement benefits. The bankruptcy or insolvency of a major competitor could result in that company s eliminating or reducing some or all of these obligations, which could give that competitor a cost advantage over us.

A disruption in supply or a significant increase in price of raw materials or parts could impact our production and increase our costs.

We concentrate our purchases of certain raw materials and parts over a limited number of suppliers. Some of these suppliers are located in developing countries, and some have experienced weakening financial strength in recent years that resulted, for some companies, in filing for protection under the bankruptcy laws.We are dependent upon the ability of our suppliers to meet performance and quality specifications and delivery schedules. The inability of a supplier to meet these requirements, the loss of a significant supplier, or any labor issues or work stoppages at a significant supplier, could disrupt the supply of raw materials and parts to our facilities and could have an adverse effect on us.

In addition, prices of raw materials, primarily steel and oil, for our business segments' manufacturing needs negatively impacted our operating income in fiscal year 2006. Although we have had some success in recovering a portion of higher steel prices from our customers, the price of steel, net of recoveries, continues to challenge our industry. We cannot predict the availability or price of steel in fiscal year 2007 and beyond. If steel supplies are inadequate for our needs, or if prices remain at current levels or increase and we are unable to either pass these prices to our customer base or otherwise mitigate the costs, our operating income could continue to be adversely affected.

Work stoppages or similar difficulties could significantly disrupt our operations.

A work stoppage at one or more of our manufacturing facilities could have material adverse effects on our business. In addition, if a significant customer were to experience a work stoppage, that customer could halt or limit purchases of our products, which could result in shutting down the related manufacturing facilities. Also, a significant disruption in the supply of a key component due to a work stoppage at one of our suppliers could result in shutting down manufacturing facilities, which could have a material adverse effect on our financial results.

Our international operations are subject to a number of risks.

We have a significant amount of facilities and operations outside the United States, including investments and joint ventures in developing countries. These international operations are subject to a number of risks inherent in operating abroad, including, but not limited to:

- risks with respect to currency exchange rate fluctuations;
- local economic and political conditions;
- disruptions of capital and trading markets;
- possible terrorist attacks or acts of aggression that could affect vehicle production or the availability of raw materials or supplies;
- restrictive governmental actions (such as restrictions on transfer of funds and trade protection measures, including export duties and quotas and customs duties and tariffs);
- changes in legal or regulatory requirements;

- import or export licensing requirements;
- limitations on the repatriation of funds;
- difficulty in obtaining distribution and support;
- nationalization;
- the laws and policies of the United States affecting trade, foreign investment and loans;
- tax laws; and
- labor disruptions.

There can be no assurance that these risks will not have a material adverse impact on our ability to increase or maintain our foreign sales or on our financial condition or results of operations.

Our liquidity, including our access to capital markets and financing, could be constrained by our credit ratings, our ability to comply with financial covenants in our debt instruments, and our suppliers extending normal trade credit terms on our purchases.

Our corporate credit rating at Standard & Poor s is BB and at Moody s Investors Service is Ba2. Standard & Poor s has our credit ratings on credit watch with a negative outlook. There are a number of factors, including our ability to achieve the intended benefits from our announced restructuring and other strategic activities on a timely basis, that could result in further lowering of our credit ratings. The rating agencies opinions about our creditworthiness may also be affected by their views of conditions in the automotive and trucking industry generally, including their views concerning the financial condition of our major OEM customers. If the credit rating agencies perceive further weakening in the industry, they could lower our ratings. Further declines in our ratings could reduce our access to capital markets, further increase our borrowing costs and result in lower trading prices for our securities.

Our ability to borrow under our existing financing arrangements depends on our compliance with covenants in the related agreements, including covenants that require maintenance of certain financial ratios. To the extent that we are unable to maintain compliance with these requirements, due to one or more of the various risk factors discussed herein or otherwise, our ability to borrow, and our liquidity, would be adversely impacted.

Our liquidity could also be adversely impacted if our suppliers were to suspend normal trade credit terms and require payment in advance or payment on delivery of purchases. If this were to occur, we would be dependent on other sources of financing to bridge the additional period between payment of our suppliers and receipt of payments from our customers.

Our strategic initiatives may be unsuccessful, may take longer than anticipated, or may result in unanticipated costs.

Our future strategic initiatives could include divestitures, acquisitions and restructurings.

The success and timing of any future divestitures and acquisitions will depend on a variety of factors, many of which are not within our control. If we engage in acquisitions, we may finance these transactions by issuing additional debt or equity securities. The additional debt from any such acquisitions, if consummated, could increase our debt to capitalization ratio. In addition, the ultimate benefit of any acquisition would depend on our ability to successfully integrate the acquired entity or assets into our existing business and to achieve any projected synergies.

We announced restructuring plans in fiscal year 2005 and in the first quarter of fiscal year 2007, and we may undertake additional restructuring actions in the future. There is no assurance that the total costs and total cash costs associated with the current and any future restructuring will not exceed our estimates, or that we will be able to achieve the intended benefits of these restructurings.

We are exposed to environmental, health and safety and product liabilities.

Our business is subject to liabilities related to the outcome of litigation with respect to environmental and health and safety matters. In addition, we are required to comply with federal, state, local and foreign laws and regulations governing the protection of the environment and occupational health and safety, and we could be held liable for damages arising out of human exposure to hazardous substances or other environmental or natural resource damages. There is also an inherent risk of exposure to warranty and product liability claims, as well as product recalls, in the automotive and commercial vehicle industry if our products fail to perform to specifications and are alleged to cause property

damage, injury or death.

With respect to environmental liabilities, we have been designated as a potentially responsible party at seven Superfund sites, and various other lawsuits, claims and proceedings have been asserted against us alleging violations of federal, state and local environmental protection requirements or seeking remediation of alleged environmental impairments. We have established reserves for these liabilities, but the process of estimating environmental liabilities is complex and dependent on physical and scientific data at the site, uncertainties as to remedies and technologies to be used, and the outcome of discussions with regulatory agencies. The actual amount of costs or damages for which we may be held responsible could materially exceed our current estimates because of a number of uncertainties that make it difficult to predict actual costs accurately. In future periods, new laws and regulations, changes in remediation plans, advances in technology and additional information about the ultimate clean-up remedy could significantly change our estimates, and management cannot assess the possible effect of compliance with future requirements.

We are exposed to asbestos litigation liability.

One of our subsidiaries, Maremont Corporation, manufactured friction products containing asbestos from 1952 through 1977, when it sold its friction product business. We acquired Maremont in 1986. Maremont and many other companies are

defendants in suits brought by individuals claiming personal injuries as a result of exposure to asbestos-containing products. We, along with many other companies, have also been named as a defendant in lawsuits alleging personal injury as a result of exposure to asbestos used in certain components of Rockwell products. Liability for these claims was transferred to us at the time of the spin-off of the automotive business to Meritor from Rockwell in 1997.

The uncertainties of asbestos claim litigation and resolution of the litigation with insurance companies make it difficult to predict accurately the ultimate resolution of asbestos claims. The possibility of adverse rulings or new legislation affecting asbestos claim litigation or the settlement process increases that uncertainty. Although we have established reserves to address asbestos liability and corresponding recoveries from insurance companies, if the assumptions with respect to the nature or pending claims, the cost to resolve claims and the amount of available insurance prove to be incorrect, the actual amount of liability for asbestos-related claims, and the effect on us, could differ materially from our current estimates and, therefore, could have a material impact on our financial position and results of operations.

We are exposed to the rising cost of pension and other post-retirement benefits, and are currently involved in litigation the outcome of which could further increase these costs.

The automotive and commercial vehicle industry, like other industries, continues to be impacted by the rising cost of pension and other post-retirement benefits. In estimating our expected obligations under the pension and post-retirement benefit plans, we make certain assumptions as to economic and demographic factors, such as discount rates, investment returns and health care cost trends. If actual experience as to these factors is worse than our assumptions, our obligations could increase. In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 (SFAS 158), Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R) . This statement requires an entity to recognize the funded status of its defined benefit pension plans and other postretirement benefit plans, such as a retiree health care plan, on the balance sheet and to recognize changes in the funded status, that arise during the period but are not recognized as components of net periodic benefit cost, within other comprehensive income, net of income taxes. SFAS 158 is effective for recognition of the funded status of the plans for fiscal years ending after December 15, 2006. When adopted, SFAS 158 will have an immediate adverse impact on the book value of our equity.

To partially address the impact of rising post-retirement benefit costs, we amended certain retiree medical plans in fiscal years 2002 and 2004, to phase out current benefits by no later than fiscal year 2023, and to eliminate benefits for Medicare eligible retirees beginning in January 2006.

Three separate class action lawsuits were filed in the United States District Court for the Eastern District of Michigan against us as a result of these amendments. The lawsuits allege that the changes breach the terms of various collective bargaining agreements entered into with the United Auto Workers (the UAW lawsuit) and the United Steel Workers (the USW lawsuit) at facilities that have either been closed or sold, and allege a companion claim restating these claims and seeking to bring them under the Employee Retirement Income Security Act of 1974.

On December 22, 2005, the court issued an order granting a motion by the United Auto Workers for a preliminary injunction. The order enjoined us from implementing the changes to retiree health benefits that had been scheduled to become effective on January 1, 2006, and ordered us to reinstate and resume paying the full cost of health benefits for the United Auto Workers retirees at the levels existing prior to the changes approved in 2002 and 2004. On August 17, 2006, the District Court granted a motion by the UAW for summary judgment; ordered the defendants to reimburse the plaintiffs for out-of-pocket expenses incurred since the date of the earlier modifications to benefits; and granted the UAW s request to make the terms of the preliminary injunction permanent.

Due to the uncertainty related to the UAW lawsuit and because the injunction has the impact of at least temporarily changing the benefits provided under the existing post-retirement medical plans, we have accounted for the injunction as a rescission of the 2002 and 2004 plan amendments that modified UAW retiree healthcare benefits. We recalculated the accumulated postretirement benefit obligation, or APBO, as of December 22, 2005, which resulted in an increase in the APBO of $168 million. The increase in APBO will offset the remaining unamortized

negative prior service cost of the 2002 and 2004 plan amendments and will increase retiree medical expense over the average remaining service period associated with the original plan amendments of approximately 10 years. In addition, the increase in APBO resulted in higher interest cost, a component of retiree medical expense. We began recording the impact of the injunction in March 2006, 90 days from the December 22, 2005 measurement date, which is consistent with the 90-day lag between our normal plan measurement date of June 30 and our fiscal year-end. In addition, the injunction required the defendants to reimburse the plaintiffs for out-of-pocket expenses incurred since the date of the earlier benefit modifications. We recorded a $5 million reserve at September 30, 2006 as the best estimate of our liability for these retroactive benefits. Including the estimated liability for retroactive benefits, the accounting for the injunction increased our retiree medical expense by approximately $17 million in fiscal year 2006. We have appealed the District Court s order to the U.S. Court of Appeals for the Sixth Circuit. The ultimate outcome of the UAW lawsuit may result in future plan amendments. The impact of any future plan amendments cannot be currently estimated.

Based on management s assessment of the USW lawsuit, the 2002 and 2004 plan amendments are still in effect for USW retirees. The ultimate outcome of the USW lawsuit may result in future plan amendments. The impact of any future plan amendments cannot be currently estimated.

Item 1B. ***Unresolved Staff Comments.***

None.

Item 2. ***Properties.***

At September 30, 2006, our operating segments and discontinued operations and our joint ventures had the following facilities in the United States, Europe, South America, Canada, Mexico, Australia, South Africa and the Asia/Pacific region:

	Manufacturing Facilities	**Engineering Facilities, Sales Offices, Warehouses and Service Centers**
LVS	67	15
CVS	34	32
LVA	10	7
Other	1	4
	112	58

These facilities had an aggregate floor space of approximately 23.3 million square feet, substantially all of which is in use. We owned approximately 77% and leased approximately 23% of this floor space. Substantially all of our domestic plants and equipment are subject to liens securing our obligations under our $1.15 billion credit facilities with a group of banks (see Note 16 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data*). In the opinion of management, our properties have been well maintained, are in sound operating condition and contain all equipment and facilities necessary to operate at present levels. A summary of floor space of these facilities at September 30, 2006, is as follows:

	Owned Facilities				**Leased Facilities**				
Location	**LVS**	**CVS**	**LVA**	**Other**	**LVS**	**CVS**	**LVA**	**Other**	**Total**
	(in thousands of square feet)								
United States	2,088	2,683	397	742	641	1,280	11		7,842
Canada	454	413			88	173	20		1,148
Europe	2,429	3,179	1,167		1,091	196	597	1	8,660
Asia/Pacific	201	471			248	544	100		1,564
Latin America	1,445	2,011	108		104	56	156		3,880
Africa	238								238
Total	6,855	8,757	1,672	742	2,172	2,249	884	1	23,332

Item 3. ***Legal Proceedings***

1. See Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations Overview* and Note 20 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* for information with respect to three class action lawsuits filed against the company as a result of modifications made to its retiree medical benefits.

2. On October 5, 2006, ZF Meritor LLC, a joint venture between an ArvinMeritor subsidiary and ZF Friedrichshafen AG, filed a lawsuit against Eaton Corporation in the United States District Court for the District of Delaware, alleging that Eaton had engaged in exclusionary, anticompetitive conduct in the markets for heavy-duty truck transmissions, in violation of the U.S. antitrust laws. The plaintiffs seek an injunction prohibiting Eaton from engaging in such anticompetitive conduct and monetary damages.

3. See Note 23 of the Notes to Consolidated Financial Statements under Item 8. *Financial Statements and Supplementary Data* for information with respect to litigation related to alleged asbestos-related liabilities.

4. See Item 1. *Business*, Environmental Matters for information relating to environmental proceedings.

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5. Various other lawsuits, claims and proceedings have been or may be instituted or asserted against ArvinMeritor or our subsidiaries relating to the conduct of our business, including those pertaining to product liability, intellectual property, safety and health, and employment matters. Although the outcome of litigation cannot be predicted with certainty and some lawsuits, claims or proceedings may be disposed of unfavorably to ArvinMeritor, management believes, after consulting with Vernon G. Baker, II, Esq., ArvinMeritor's General Counsel, that the disposition of matters that are pending will not have a material adverse effect on our business, financial condition or results of operations.

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

There were no matters submitted to a vote of security holders during the fourth quarter of fiscal year 2006.

Item 4A. ***Executive Officers of the Registrant***.

The name, age, positions and offices held with ArvinMeritor and principal occupations and employment during the past five years of each of our executive officers as of October 31, 2006, are as follows:

Charles G. McClure, Jr., 53 - Chairman of the Board, Chief Executive Officer and President since August 2004. Chief Executive Officer of Federal-Mogul Corporation (automotive component supplier) from July 2003 to July 2004; President and Chief Operating Officer of Federal-Mogul Corporation from January 2001 to July 2003.

Vernon G. Baker, II, 53 - Senior Vice President and General Counsel since July 2000.

Jeffrey A. Craig, 46 Vice President and Controller since May 2006. President and Chief Executive Officer, Commercial Finance, of General Motors Acceptance Corporation (automotive and commercial finance, mortgage, real estate and insurance businesses) from 2001 to May 2006.

Linda M. Cummins, 59 - Senior Vice President, Communications, since July 2000.

James D. Donlon, III, 60 - Senior Vice President and Chief Financial Officer since April 2005. Senior Vice President and Chief Financial Officer of Kmart Corporation (retailer) from January 2004 to March 2005; Senior Vice President and Controller of the Chrysler Division of DaimlerChrysler AG (automotive) from 2001 to 2003.

Mary A. Lehmann, 47 Vice President and Treasurer since January 2006. Assistant Treasurer of ArvinMeritor from 2004 to January 2006; Director, Affiliate Financing, of Ford Motor Company (automotive) from 2001 to 2004.

Perry L. Lipe, 60 - Senior Vice President and Chief Information Officer since July 2000.

Philip R. Martens, 46 Senior Vice President and President, Light Vehicle Systems, since September 2006. President and Chief Operating Officer of Plastech Engineered Products, Inc. (automotive component supplier) from 2005 to 2006; Group Vice President, Product Creation, of Ford Motor Company (automotive) from 2003 to 2005; Vice President, North American Product Creation, of Ford Motor Company in 2003;Vice President, North American Product Development of Ford Motor Company from 2002 to 2003; and Managing Director, Planning, Design and Product Development of Mazda Motor Company (automotive) from 1999 to 2002.

Robert Ostrov, 57 Senior Vice President, Human Resources, since September 2006. Vice President, Human Resources and Labor Relations, of FedEx Ground Package System, Inc. (shipping services), a subsidiary of FedEx Corporation, from 2005 to September 2006; Attorney, Arnold & Partners, from February 2003 to 2005; Senior Vice President, Human Resources, of TruServ Corporation (now True Value Company) (hardware, plumbing and heating supplies) from 1997 to February 2003.

Carsten J. Reinhardt, 39 Senior Vice President and President, Commercial Vehicle Systems since September 2006. Chief Executive Officer and President of Detroit Diesel Corporation (a subsidiary of DaimlerChrysler AG) from March 2003 to August 2006; Plant Manager of the Portland Truck Manufacturing Plant of Freightliner LLC/Western Star Trucks (subsidiaries of DaimlerChrysler AG) from October 2002 to February 2003; Vice President and General Manager, Operations, of Western Star Trucks from March 2001 to September 2002.

Rakesh Sachdev, 50 Senior Vice President, Corporate Development and Strategy, since April 2005. Vice President and Controller of ArvinMeritor from August 2003 to March 2005; Vice President and General Manager, Worldwide Braking Systems, of ArvinMeritor from December 2000 to July 2003.

H. H. Buddy Wacaser, 57 Senior Vice President and President, Emissions Technology Group, since September 2006. President and Chief Executive Officer of Meridian Automotive Systems, Inc. (automotive component supplier) from 2002 to 2005; Executive Vice President of Meridian Automotive Systems, Inc. from 1997 to 2002.

Bonnie Wilkinson, 56 Vice President and Secretary since November 2001.

There are no family relationships, as defined in Item 401 of Regulation S-K, between any of the above executive officers and any director, executive officer or person nominated to become a director or executive officer. No officer of ArvinMeritor was selected pursuant to any arrangement or understanding between him or her and any person other than ArvinMeritor. All executive officers are elected annually.

PART II

Item 5. ***Market for the Registrant s Common Equity and Related Stockholder Matters*.**

ArvinMeritor's common stock, par value $1 per share (Common Stock), is listed on the New York Stock Exchange (NYSE) and trades under the symbol "ARM." On October 31, 2006, there were 27,504 shareowners of record of ArvinMeritor's Common Stock.

The high and low sale prices per share of ArvinMeritor Common Stock for each quarter of fiscal years 2006 and 2005 were as follows:

	Fiscal Year 2006		Fiscal Year 2005	
Quarter Ended	**High**	**Low**	**High**	**Low**
December 31	$ 17.28	$ 12.67	$ 22.83	$ 16.25
March 31	17.68	13.21	22.62	15.15
June 30	17.90	14.52	19.92	11.74
September 30	17.36	13.37	20.22	15.70

Quarterly cash dividends in the amount of $0.10 per share were declared and paid in each quarter of the last two fiscal years.

See Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters* for information on securities authorized for issuance under equity compensation plans.

On August 7, 2006, the company issued 11,400 shares of Common Stock to a retiring non-employee director in settlement of restricted share units that were awarded to him in 2004, 2005 and 2006 as annual grants under the 2004 Directors Stock Plan. The issuance of these securities was exempt from registration under the Securities Act of 1933, as a transaction not involving a public offering under Section 4(2).

Item 6. ***Selected Financial Data***.

The following sets forth selected consolidated financial data. Prior period amounts have been restated for discontinued operations. The data should be read in conjunction with the information included under Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations* and Item 8. *Financial Statements and Supplementary Data* below.

	Year Ended September 30,				
SUMMARY OF OPERATIONS	**2006**	**2005**	**2004**	**2003**	**2002**
Sales					
Light Vehicle Systems	$ 4,905	$ 4,819	$ 4,672	$ 4,058	$ 3,309
Commercial Vehicle Systems	4,290	4,054	3,215	2,422	2,249
Total	$ 9,195	$ 8,873	$ 7,887	$ 6,480	$ 5,558
Income (Loss) from Continuing Operations (1)	$ (174)	$ 63	$ 117	$ 105	$ 104
Income (Loss) from Discontinued Operations (2)	(1)	(51)	(159)	32	45
Income (Loss) Before Cumulative Effect of Accounting Change	(175)	12	(42)	137	149
Cumulative Effect of Accounting change				(4)	(42)
Net Income (Loss)	$ (175)	$ 12	$ (42)	$ 133	$ 107
BASIC EARNINGS (LOSS) PER SHARE					
Continuing Operations (1)	$ (2.51)	$ 0.92	$ 1.74	$ 1.58	$ 1.56
Discontinued Operations (2)	(0.01)	(0.75)	(2.36)	0.47	0.68
Cumulative Effect of Accounting Change				(0.06)	(0.63)
Basic Earnings (Loss) per Share	$ (2.52)	$ 0.17	$ (0.62)	$ 1.99	$ 1.61
DILUTED EARNINGS (LOSS) PER SHARE					
Continuing Operations (1)	$ (2.51)	$ 0.90	$ 1.71	$ 1.55	$ 1.55
Discontinued Operations (2)	(0.01)	(0.73)	(2.32)	0.47	0.67
Cumulative Effect of Accounting Change				(0.06)	(0.63)
Diluted Earnings (Loss) per Share	$ (2.52)	$ 0.17	$ (0.61)	$ 1.96	$ 1.59
Cash Dividends per Share	$ 0.40	$ 0.40	$ 0.40	$ 0.40	$ 0.40
FINANCIAL POSITION AT SEPTEMBER 30					
Total Assets	$ 5,513	$ 5,870	$ 5,639	$ 5,448	$ 4,717
Short-term Debt	56	136	5	19	15
Long-term Debt	1,184	1,451	1,487	1,541	1,473

(1) Fiscal year 2006 loss from continuing operations includes a $310 million ($310 million after-tax) non-cash goodwill impairment charge, $37 million ($23 million after-tax) of restructuring charges, gains on divestitures of $28 million ($17 million after-tax) and environmental rememdiation charges of $8 million ($5 million after-tax). Fiscal year 2005 income from continuing operations includes restructuring charges of $86 million ($53 million after-tax), charges associated with certain customer bankruptcies of $14 million ($9 million after-tax), environmental charges of $7 million ($4 million after-tax), and a gain on divestitures of $4 million ($3 million after-tax). Fiscal year 2004 income from continuing operations include restructuring charges of $15 million ($11 million after-tax), environmental remediation charges of $11 million ($8 million after-tax), a withdrawn tender offer net charge of $9 million ($6 million after-tax). Fiscal year 2003 income from continuing operations include restructuring charges of $20 million ($14 million after-tax) and a gain on divestitures of $15 million ($11 million after-tax). Fiscal year 2002 income from continuing operations includes restructuring charges of $11 million ($8 million after-tax).

(2) Fiscal year 2006 includes a net gain on the sale of certain LVA businesses of $28 million ($18 million after-tax) and non-cash impairment charges of $22 million ($14 million after-tax) to record certain North American LVA businesses at fair value. Fiscal year 2005 includes a non-cash impairment charge of $43 million ($28 million after-tax) to record certain North American LVA businesses at fair value. Fiscal year 2004 includes a non-cash goodwill impairment charge of $190 million in our LVA business.

Item 7. ***Management s Discussion and Analysis of Financial Conditions and Results of Operations.***
Overview

ArvinMeritor, Inc. is a global supplier of a broad range of integrated systems, modules and components to the motor vehicle industry. The company serves light vehicle, commercial truck, trailer and specialty original equipment manufacturers and certain aftermarkets. Headquartered in Troy, Michigan, the company employs approximately 27,500 people at 112 manufacturing facilities in 26 countries. ArvinMeritor common stock is traded on the New York Stock Exchange under the ticker symbol ARM.

During fiscal year 2006, we completed the following transactions, which significantly improved our financial strength and liquidity position.

Issued $300 million of 4.625 percent convertible senior unsecured notes due 2026, with an earlier redemption option beginning in 2016;
Replaced our $900 million revolving credit facility that was to expire in 2008 with two new senior secured credit facilities totaling $1.15 billion. The new c
Purchased and extinguished $672 million of fixed term debt with maturities ranging from 2007 though 2012, resulting in no significant fixed-term debt ma
Sold our LVA North American filters, exhaust and motion control businesses, our Gabriel South Africa ride control business, and our 39 percent interest in
Increased our European accounts receivable securitization and factoring programs, resulting in total availability of $300 million.

In fiscal year 2006, our light vehicle emissions technologies business continued to face significant challenges, including higher raw material costs, intense pricing pressures and increased competition. These factors were greater than previously anticipated and partially offset the expected benefits from our fiscal year 2005 restructuring actions. In addition, higher stainless steel prices and recent downturns in production at certain North American manufacturers are expected to further negatively impact the financial performance of this business in fiscal year 2007. These combined factors resulted in a decline in the fair value of the light vehicle emissions technologies business in fiscal year 2006, and accordingly, we recorded a $310 million non-cash goodwill impairment charge in the fourth quarter of fiscal year 2006. In response to these challenges we continue to rationalize and restructure this business. We are merging our light and commercial vehicle emissions businesses into a combined Emissions Technologies (ET) business and beginning in fiscal year 2007, ET will be a separate reportable segment. We have also identified restructuring plans to downsize certain facilities and realign our manufacturing footprint to utilize assets more efficiently, improve operations and lower costs. The total estimated cost of these actions is $50 million, of which approximately $40 million is expected to be cash costs. This restructuring program will be executed over the next 12 to 36 months. No amounts have been recorded for this restructuring program at September 30, 2006.

Our financial results for fiscal year 2006 were favorably impacted by strong volumes in the principal markets served by our Commercial Vehicle Systems (CVS) business. These results were negatively impacted by a labor disruption and work stoppage at our commercial vehicle brakes facility in Tilbury, Ontario, Canada in the third quarter of fiscal year 2006. In June 2006, a tentative collective bargaining agreement with the Canadian Auto Workers (CAW) could not be reached and, as a result, operations at the facility were suspended. An agreement with the CAW was eventually reached and operations resumed. This labor disruption negatively impacted operating income during fiscal year 2006 by $45 million. Included in this amount are premium labor costs, expedited freight and logistical costs and other costs associated with production disruptions at certain customers facilities.

A summary of our results for the fiscal year ended September 30, 2006 is as follows:

Sales were $9.2 billion, up 4 percent from a year ago.
Operating margins were negative 1.3 percent, down from 2.1 percent a year ago. Fiscal year 2006 operating margins were significantly impacted by the $3
Basic and diluted loss per share from continuing operations was $2.51, compared to earnings of $0.90 per diluted share in fiscal year 2005.
Basic and diluted loss per share from discontinued operations were $0.01, compared to $0.73 per diluted share in the prior year.
Net loss was $175 million or $2.52 per basic and diluted share, compared to net income of $12 million, or $0.17 per diluted share in the prior year.
We continue to execute our restructuring plans announced in early fiscal year 2005 and recorded $37 million of restructuring costs, primarily in our LVS business segment, in fiscal year 2006. To date, we have downsized, consolidated, closed or sold 11 facilities, primarily in the LVS business segment.

Higher raw material costs and intense competition, coupled with global excess capacity most notably in the light vehicle industry, have created pressure from customers to reduce our prices. We continuously work to address these competitive challenges and offset price decreases by reducing costs, improving productivity and restructuring operations. The company s cost reduction and productivity programs, including savings from our restructuring actions, more than offset the impact of lower selling prices to our customers in fiscal year 2006.

Also impacting our industry is the rising cost of pension and other post-retirement benefits. To partially address this issue we approved amendments to certain retiree medical plans in fiscal years 2002 and 2004. The cumulative effect of these amendments was a reduction in the accumulated postretirement benefit obligation (APBO) of $293 million, which was being amortized as a reduction of retiree medical expense over the average remaining service period of approximately 12 years. These plan amendments have been challenged in three separate class action lawsuits filed in the United States District Court for the Eastern District of Michigan (District Court). The lawsuits allege that the changes breach the terms of various collective bargaining agreements entered into with the United Auto Workers (the UAW lawsuit) and the United Steel Workers (the USW lawsuit) at facilities that have either been closed or sold. Plaintiffs in the UAW lawsuit sought injunctive relief requiring the company to provide lifetime retiree health care benefits under the applicable collective bargaining agreements. On December 22, 2005, the District Court issued an order granting a motion by the UAW for a preliminary injunction. The order enjoined the company from implementing the changes to retiree health benefits that had been scheduled to become effective on January 1, 2006, and ordered the company to reinstate and resume paying the full cost of health benefits for the UAW retirees at the levels existing prior to the changes approved in 2002 and 2004. On August 17, 2006, the District Court denied a motion by the company and the other defendants for summary judgment; granted a motion by the UAW for summary judgment; and granted the UAW s request to make the terms of the preliminary injunction permanent (the injunction). Due to the uncertainty related to the ongoing lawsuits and because the injunction has the impact of at least temporarily changing the benefits provided under the existing postretirement medical plans, we have accounted for the injunction as a rescission of the 2002 and 2004 plan amendments that modified UAW retiree healthcare benefits. In addition, the injunction ordered the defendants to reimburse the plaintiffs for out-of-pocket expenses incurred since the date of the earlier benefit modifications. We recorded a $5 million reserve at September 30, 2006 as the best estimate of our liability for these retroactive benefits. Including the estimated liability for retroactive benefits, the accounting for the injunction increased retiree medical expense by approximately $17 million in fiscal year 2006. We continue to believe we have meritorious defenses to these actions and have appealed the District Court s order to the U.S. Court of Appeals for the Sixth Circuit. The ultimate outcome of the UAW lawsuit may result in future plan amendments. The impact of any future plan amendments cannot be currently estimated. Based on management s assessment of the USW lawsuit, the 2002 and 2004 plan amendments are still in effect for USW retirees. The ultimate outcome of the USW lawsuit may result in future plan amendments. The impact of any future plan amendments cannot be currently estimated.

We previously announced our intention to divest our Light Vehicle Aftermarket (LVA) businesses and therefore these businesses are reported as discontinued operations for all periods presented. As previously mentioned, we sold our LVA North American filters, exhaust and motion control businesses, our Gabriel South Africa ride control business and our 39 percent interest in our Purolator India joint venture during fiscal year 2006, generating cash proceeds of approximately $220 million. These businesses represented a significant portion of our combined LVA business and we expect to complete the divestiture of our remaining LVA businesses in fiscal year 2007.

In December 2005, we sold our light vehicle ride control business located in Asti, Italy. This sale, along with the previous divestiture of our 75-percent interest in AP Amortiguadores, S.A. (APA) in the second quarter of fiscal year 2004, substantially

completed our plan to exit the LVS ride control business. Therefore, the results of operations of this business are included in discontinued operations for all periods presented.

Cash provided by operating activities for the fiscal year ended September 30, 2006 was $440 million, compared to $32 million of cash used by operating activities in the prior year. The increase in cash flow was largely driven by a reduction in working capital, including non-recourse sales of accounts receivable, and lower pension and retiree medical contributions of $50 million.

MARKET OUTLOOK

Historically, the company has experienced periodic fluctuations in demand for light, commercial and specialty vehicles and certain aftermarkets, most notably in our commercial vehicle markets in North America. Vehicle production in our principal markets for the last five fiscal years is shown below:

	Year Ended September 30				
	2006	**2005**	**2004**	**2003**	**2002**
Light Vehicles (in millions):					
North America	15.7	15.6	15.9	16.0	16.3
South America	3.0	2.7	2.3	2.0	1.9
Western Europe (including Czech Republic)	16.4	16.4	16.9	16.7	16.5
Asia/Pacific	24.8	22.7	20.9	18.9	17.3
Commercial Vehicles (in thousands):					
North America, Heavy-Duty Trucks	352	324	235	164	169
North America, Medium-Duty Trucks	216	208	172	141	133
United States and Canada, Trailers	312	327	284	213	145
Western Europe, Heavy- and Medium-Duty Trucks	439	421	376	364	363
Western Europe, Trailers	118	115	109	98	101

Source: Automotive industry publications and management estimates.

We anticipate the North American heavy-duty truck market to decrease approximately 33% in fiscal year 2007, with production at an estimated 235,000 units. In Western Europe, we expect production of heavy- and medium-duty trucks to be approximately 419,000 units. Our most recent outlook shows North American and Western European light vehicle production during fiscal year 2007 to be about the same as fiscal year 2006.

COMPANY OUTLOOK

Our business continues to address a number of challenging industry-wide issues, including:

- Excess capacity;
- High commodity prices, particularly steel and oil prices;
- Weakened financial strength of some of the original equipment (OE) manufacturers;
- Employee labor relations;
- Reduced production volumes and changes in product mix in North America;
- Higher energy and transportation costs;
- OE pricing pressures; and
- Currency exchange rate volatility.

We believe the price of steel will continue to challenge our industry during fiscal year 2007. While we generally do not expect this issue to significantly impact our results of operations when compared to the prior year, rising stainless steel prices are expected to negatively impact earnings. We have taken actions to help mitigate this issue, including finding new global steel sources, identifying alternative materials, finding

ways to re-engineer our products to be less dependent on steel, working with our suppliers to reduce material costs, consolidating and selling scrap from many of our facilities and negotiating with our customers to recover some of the higher steel costs. We continue to further consolidate and restructure our LVS business to address competitive challenges in the automotive supplier industry. Anticipated restructuring actions include those actions previously discussed.

Significant factors that could affect our results in fiscal year 2007 include:

- Higher than planned price reductions to our customers;
- Additional restructuring actions and the timing and recognition of restructuring charges;
- Our ability to recover steel price increases from our customers;
- The financial strength of our suppliers and customers, including potential bankruptcies;
- Any unplanned extended shutdowns or production interruptions;
- Our ability to implement planned productivity and cost reduction initiatives;
- The impact of any acquisitions or divestitures;
- Significant gains or losses of existing business;
- The ultimate outcome of the three class action lawsuits concerning our retiree medical plans;
- The impact of currency fluctuations on sales and operating income;
- The emergence from bankruptcy of certain competitors;
- Higher than planned warranty expenses;
- Any adjustments to the contingent liability associated with the Tilbury labor disruption;
- Our ability to continue to access our bank revolving credit facilities and capital markets;
- A significant reduction of business activity in the key markets of our customers;
- The expected 2007 Class 8 downturn in North America or Europe is more severe than currently planned;
- Lower volume of orders from key customers;
- Ability to implement enterprise resource planning systems at our location successfully; and
- The impact of any new accounting rules.

Results of Operations

The following is a summary of our financial results for the last three fiscal years. Prior period amounts have been restated for discontinued operations.

	Year Ended September 30,		
	2006	2005	2004
	(in millions, except per share amounts)		
Sales:			
Light Vehicle Systems	$4,905	$4,819	$4,672
Commercial Vehicle Systems	4,290	4,054	3,215
SALES	9,195	8,873	7,887
Operating Income (Loss):			
Light Vehicle Systems	$(291)	$1	$118
Commercial Vehicle Systems	185	193	164
SEGMENT OPERATING INCOME (LOSS)	(106)	194	282
Environmental remediation costs	(8)	(7)	(11)
Costs for withdrawn tender offer			(16)
Other unallocated corporate costs	(5)	(3)	
OPERATING INCOME (LOSS)	(119)	184	255
Equity in earnings of affiliates	36	28	19
Gain on sale of marketable securities			7
Interest expense, net and other	(133)	(127)	(107)
INCOME (LOSS) BEFORE INCOME TAXES	(216)	85	174
Benefit (provision) for income taxes	56	(16)	(46)
Minority interests	(14)	(6)	(11)
INCOME (LOSS) FROM CONTINUING OPERATIONS	(174)	63	117
LOSS FROM DISCONTINUED OPERATIONS, net of tax	(1)	(51)	(159)
NET INCOME (LOSS)	$(175)	$12	$(42)
DILUTED EARNINGS (LOSS) PER SHARE			
Continuing operations	$(2.51)	$0.90	$1.71
Discontinued operations	(0.01)	(0.73)	(2.32)
Diluted earnings (loss) per share	$(2.52)	$0.17	$(0.61)
DILUTED AVERAGE COMMON SHARES OUTSTANDING	69.3	69.9	68.6

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2006 Compared to 2005

Sales

The following table reflects geographical business segment sales for fiscal years 2006 and 2005. The reconciliation is intended to reflect the trend in business segment sales and to illustrate the impact changes in foreign currency exchange rates and acquisitions and divestitures had on sales (in millions).

					Dollar Change Due to		
	2006	**2005**	**Dollar Change**	**% Change**	**Currency**	**Acquisitions Divestitures**	**Volume / Other**
LVS:							
North America	$1,902	$2,042	$(140)	(7)%	$16	$(14)	$(142)
Europe	2,405	2,209	196	9%	(75)	(10)	281
Asia and Other	598	568	30	5%	19		11
Total	4,905	4,819	86	2%	(40)	(24)	150
CVS:							
North America	2,707	2,475	232	9%	5	(41)	268
Europe	1,094	1,106	(12)	(1)%	(57)	(16)	61
Asia and Other	489	473	16	3%	20		(4)
Total	4,290	4,054	236	6%	(32)	(57)	325
SALES	$9,195	$8,873	$322	4%	$(72)	$(81)	$475

Continuing Operations

Sales for fiscal year 2006 were $9,195 million, up $322 million, or 4 percent, from fiscal year 2005. The increase in sales was attributable to strong commercial vehicle truck and trailer volumes in our CVS business segment and higher pass-through sales in our LVS business segment. These increases were partially offset by foreign currency translation, primarily due to the stronger euro in relation to the U.S. dollar, which reduced sales by $72 million, and lower volumes in our North American LVS businesses. Divestitures of certain LVS businesses in previous periods and the sale of certain assets of CVS off-highway brake business reduced sales in fiscal year 2006 by $81 million.

Business Segments

Light Vehicle Systems (LVS) sales increased to $4,905 million in fiscal year 2006, up $86 million, or 2 percent, from $4,819 million in fiscal year 2005. The effect of foreign currency translation decreased sales by $40 million. Pass-through sales were approximately $1,600 million in fiscal year 2006 compared to approximately $1,300 million in fiscal year 2005. The higher pass-through sales were partially offset by lower value added sales, lower selling prices to our customers and the loss of sales associated with previously announced divestitures. Pass-through sales are products sold to our customers where we acquire certain components and assemble them into the final product. These pass-through sales carry minimal margins, as we have little engineering or manufacturing responsibility.

Commercial Vehicle Systems (CVS) sales were $4,290 million, up $236 million, or 6 percent, from fiscal year 2005. The increase in sales was primarily attributable to strong commercial vehicle truck and trailer volumes. Compared to fiscal year 2005, production volumes in North America for commercial vehicle heavy-duty trucks (Class 8) increased 8 percent and medium duty trucks increased 4 percent. Western Europe heavy and medium duty truck volumes increased 4 percent. These increases were partially offset by the loss of sales associated with the

divestiture of certain assets of the off-highway brakes business of approximately $57 million and foreign currency translation which reduced sales by $32 million.

Operating Income (Loss) and Operating Margins

The following table reflects operating income and operating margins for fiscal years 2006 and 2005 (dollars in millions).

	Operating Income				Operating Margins			
	2006	2005	$ Change	% Change	2006	2005	Change	
LVS	$(291)	$1	$(292)		(5.9)%	0.0%	(5.9)	pts
CVS	185	193	(8)	(4)%	4.3%	4.8%	(0.5)	pts
Total Segment	(106)	194	(300)	(155)%	(1.2)%	2.2%	(3.4)	pts
Unallocated corporate costs	(13)	(10)	(3)	30%				
	$(119)	$184	$(303)	(165)%	(1.3)%	2.1%	(3.4)	pts

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Operating loss for fiscal year 2006 was $119 million, compared to operating income of $184 million in fiscal year 2005. Operating loss was significantly impacted by a $310 million non-cash goodwill impairment charge recorded in our light vehicle emissions technologies business in the fourth quarter of fiscal year 2006. A labor disruption and work stoppage at our commercial vehicle brakes operation in Tilbury, Ontario unfavorably impacted operating income by $45 million. Operating loss for fiscal year 2006 also includes a $23 million gain on the sale of certain assets of CVS off-highway brakes business.

We recorded restructuring costs during fiscal years 2006 and 2005 as follows (in millions):

	LVS		CVS		Total	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
Fiscal year 2005 program (1):						
Salaried reduction force	$22	$10	$	$13	$22	$23
Facility rationalization, primarily employee severance benefits	18	30	7	6	25	36
Asset impairment	3	11			3	11
Reversals	(12)		(1)		(13)	
Total fiscal year 2005 program	31	51	6	19	37	70
Other actions		16				16
Total restructuring costs	$31	$67	$6	$19	$37	$86

(1) The fiscal year 2005 program relates to the restructuring actions announced in May 2005.

The benefit of higher sales levels in our CVS business and cost savings from our restructuring actions of $29 million were largely offset by the loss of income associated with certain of our previous divestitures of approximately $20 million and higher pension and retiree medical costs of $32 million when compared to the same period last year. Impacting operating income in fiscal year 2005 were $14 million of charges associated with certain customer bankruptcies; $7 million of environmental remediation costs, primarily associated with a former Rockwell facility; and a $4 million gain on the sale of an automotive stamping and components manufacturing operation in the first quarter of fiscal year 2005.

Selling, general and administrative expenses as a percentage of sales were 4.1 percent in fiscal year 2006, compared to 4.2 percent in the prior year.

Business Segments

LVS operating loss was $291 million, compared to operating income of $1 million in fiscal year 2005. The primary driver for the decrease in operating income is the $310 million non-cash goodwill impairment charge recorded in the fourth quarter of fiscal year 2006.

LVS recorded restructuring costs of $31 million in fiscal year 2006. These restructuring costs are net of reversals of costs recorded in previous periods of $12 million and include $39 million of employee termination benefits, $3 million of asset impairment charges and $1 million of other costs associated with the closure of certain facilities. In the prior year, LVS recorded restructuring costs of $67 million. These charges included $51 million of costs associated with the actions announced in the second quarter of fiscal year 2005 and $16 million associated with the closure of the Sheffield, England stabilizer bar facility, the consolidation of two facilities in Brazil and a reduction in workforce in LVS operations in Spain. The $16 million relates to employee termination benefits and other costs of $11 million and asset impairments of $5 million.

In fiscal year 2006, LVS was able to more than offset lower customer pricing with productivity and cost reduction actions and restructuring savings. Also impacting operating income in fiscal year 2006 were approximately $20 million of liabilities recorded for certain warranty and other commercial matters and $9 million of higher pension and retiree medical costs. LVS also recorded a $5 million gain on the liquidation of Meritor Suspension Systems Holding (UK) Ltd., a joint venture, in fiscal year 2006. This gain primarily related to the extinguishment of debt owed to the minority partner. Operating income in fiscal year 2005 included $11 million of charges associated with certain customer bankruptcies, a $4 million net charge associated with a product warranty matter and a $4 million gain on the sale of LVS Columbus, Indiana stamping and manufacturing components business in the first quarter of fiscal year 2005.

CVS operating income was $185 million in fiscal year 2006, down from $193 million in fiscal year 2005. Operating margin declined to 4.3 percent, from 4.8 percent in fiscal year 2005. The benefits of higher sales volumes were more than offset by the labor disruption and work stoppage at our brakes facility in Tilbury, which unfavorably impacted operating income by $45 million, approximately $24 million of liabilities for certain warranty and other commercial matters and $23 million of higher pension and retiree medical costs. Favorably impacting operating income was a $23 million gain on the sale of certain assets of the off-highway brake business, productivity and cost reduction actions and restructuring savings. CVS recorded restructuring costs of $6 million in fiscal year 2006, primarily related to employee severance benefits, compared to restructuring costs of $19 million in the prior year. Impacting fiscal year 2005 operating income was a $3 million charge associated with the bankruptcy of a European trailer customer.

Other Income Statement Items

Equity in earnings of affiliates was $36 million in fiscal year 2006, compared to $28 million in fiscal year 2005. The increase was primarily related to improved performance and higher earnings of our commercial vehicle affiliates.

Interest expense, net and other was $133 million in fiscal year 2006 compared to $127 million in fiscal year 2005. Included in interest expense, net and other in fiscal year 2006 were $9 million of costs associated with the extinguishment of $600 million of notes we repurchased in the second quarter of fiscal year 2006. These costs include transaction expenses, including legal and other professional fees, unamortized debt issuance costs, and premiums paid to repurchase the notes. Included in interest expense, net and other in fiscal year 2005 was a $4 million loss on debt extinguishment associated with the debt exchange completed in the fourth quarter of fiscal year 2005. The loss on debt extinguishment primarily consisted of the premium paid to note holders to exchange their notes. See Liquidity and Contractual Obligations for further details concerning these debt extinguishments. The favorable impact of reduced fixed rate debt was partially offset by higher levels of short term borrowings and higher interest rates on our variable rate debt compared with the prior year.

Income tax benefit from continuing operations in fiscal year 2006 was $56 million compared to income tax expense of $16 million in the prior year. In fiscal year 2006, we recorded a $23 million tax benefit related to the expiration of certain statutes of limitations and the completion of various worldwide tax audits of certain of the company s income tax returns. We also repatriated approximately $152 million in dividends in the fourth quarter of fiscal year as part of the American Jobs Creation Act of 2004. The dividends are subject to the elective 85 percent dividend received deduction and accordingly we recorded a corresponding tax benefit of $37 million related to the reversal of previously provided U.S. deferred tax liability on these unremitted foreign subsidiary earnings.

Minority interest expense was $14 million in fiscal year 2006 compared to $6 million in fiscal year 2005. Minority interests represent our minority partners share of income or loss associated with our less than 100-percent owned consolidated joint ventures. The increase in minority interest expense in fiscal year 2006 was primarily due to improved earnings in our commercial vehicle affiliates and the closure of the Sheffield, England, stabilizer bar facility in our MSSH joint venture in fiscal year 2005.

Loss from continuing operations for fiscal year 2006 was $174 million, or $2.51 per diluted share, compared to income from continuing operations of $63 million, or $0.90 per diluted share in fiscal year 2005. The decrease is primarily attributable to the $310 million goodwill impairment charge recorded in the fourth quarter of fiscal year 2006, partially offset by the income tax benefits previously mentioned.

Loss from discontinued operations was $1 million in fiscal year 2006 compared to $51 million in fiscal year 2005.

In fiscal year 2006, we completed the sale of our LVA North American filters, exhaust and motion control businesses, our Gabriel South Africa ride control business and our 39 percent interest in our Purolator India joint venture. Cash proceeds from these divestitures were approximately $220 million, resulting in a net pre-tax gain of $28 million ($18 million after-tax). We also recorded non-cash impairment charges of $22 million ($14 million after-tax) during fiscal year 2006 in certain of our LVA businesses. A non-cash impairment charge of $43 million ($28 million after-tax) related to our LVA businesses was recorded in fiscal year 2005. A $2 million after-tax gain on the sale of our coil coating business is included in income from discontinued operations in fiscal year 2005. Also impacting fiscal year 2005 were $6 million of after-tax changeover costs in LVA associated with a new supply agreement with a significant customer.

Loss from discontinued operations in fiscal years 2006 and 2005 includes after-tax restructuring costs of $4 million and $1 million, respectively, related to our LVA businesses.

Also included in loss from discontinued operations in fiscal year 2006 is an after-tax loss of $2 million on the sale of our LVS ride control business located in Asti, Italy and a reversal of approximately $7 million of after-tax employee severance benefits that were recorded in the prior year as part of our fiscal year 2005 restructuring actions. As a result of the sale of the ride control operations in Asti, Italy, these employee termination benefits will no longer be paid. Loss from discontinued operations in the prior year includes approximately $20 million of after-tax restructuring costs related to the previously expected closure of our light vehicle ride control operations.

2005 Compared to 2004

Sales

The following table reflects geographical business segment sales for fiscal years 2005 and 2004. The reconciliation is intended to reflect the trend in business segment sales and to illustrate the impact changes in foreign currency exchange rates and acquisitions and divestitures had on sales (in millions).

					Dollar Change Due to		
	2005	2004	Dollar Change	% Change	Currency	Acquisitions / Divestitures	Volume / Other
LVS:							
North America	$2,042	$1,971	$71	4%	$17	$(70)	$124
Europe	2,209	2,206	3	0%	150	(17)	(130)
Asia and Other	568	495	73	15%	35	(33)	71
	4,819	4,672	147	3%	202	(120)	65
CVS:							
North America	2,475	2,014	461	23%	4	9	448
Europe	1,106	827	279	34%	54	226	(1)
Asia and Other	473	374	99	26%	31		68
	4,054	3,215	839	26%	89	235	515
SALES	$8,873	$7,887	$986	13%	$291	$115	$580

Continuing Operations

Sales for fiscal year 2005 were $8,873 million, up $986 million, or 13 percent, over fiscal year 2004. The increase in sales was attributable to stronger commercial vehicle truck and trailer volumes in our CVS business segment; new business awards, principally associated with suspension modules in our LVS business; and foreign currency translation, primarily due to the stronger euro in relation to the U.S. dollar. These increases were partially offset by lower volumes in certain of our European LVS businesses. Acquisitions, primarily our two new consolidated joint ventures with AB Volvo, added sales of $235 million; divestitures of certain LVS businesses in fiscal years 2005 and 2004 reduced sales in fiscal year 2005 by $120 million.

Business Segments

LVS sales increased to $4,819 million in fiscal year 2005, up $147 million, or 3 percent, from fiscal year 2004. The effect of foreign currency translation, primarily as a result of the stronger euro when compared to the US dollar, increased sales by $202 million. Divestitures, primarily the sale an automotive stamping and components manufacturing operation in the first quarter of fiscal year 2005, reduced sales by $120 million. Excluding the impact of foreign currency translation and divestitures, sales were up $65 million. Higher pass-through sales of approximately $300 million, principally associated with our new suspension module business, were partially offset by lower OE demand particularly in certain of our European businesses. Pass-through sales increased to approximately $1,300 million in fiscal year 2005 from approximately $1,000 million in fiscal year 2004.

CVS sales were $4,054 million, up $839 million, or 26 percent, from fiscal year 2004. The increase in sales was primarily attributable to stronger commercial vehicle truck and trailer volumes. Compared to fiscal year 2004, production volumes in North America for commercial vehicle heavy-duty trucks (Class 8) increased approximately 38 percent, medium duty trucks increased 21 percent and trailer volumes increased 15 percent. South American truck volumes increased 17 percent. Acquisitions, primarily the formation of two joint ventures with AB Volvo in the first quarter of fiscal 2005, added sales of $235 million.

Operating Income and Operating Margins

The following table reflects operating income and operating margins for fiscal years 2005 and 2004 (dollars in millions).

	Operating Income				Operating Margins		
	2005	2004	$ Change	% Change	2005	2004	Change
LVS	$1	$118	$(117)	(99)%	0.0%	2.5%	(2.5) pts
CVS	193	164	29	18%	4.8%	5.1%	(0.3) pts
Total Segment	194	282	(88)	(31)%	2.2%	3.6%	(1.4) pts
Unallocated corporate costs	(10)	(27)	17	63%			
TOTAL	$184	$255	$(71)	(28)%	2.1%	3.2%	(1.1) pts

Operating income in fiscal year 2005 was $184 million, a decrease of $71 million, compared to fiscal year 2004, reflecting an operating margin of 2.1 percent, down from 3.2 percent. We recorded restructuring costs of $86 million during fiscal year 2005 as follows (in millions):

	LVS	CVS	Total
Fiscal year 2005 program (1):			
Facility rationalization	$ 40	$ 19	$ 59
Asset impairments	11		11
Total fiscal year 2005 program	51	19	70
Other actions	16		16
Total restructuring costs	$ 67	$ 19	$ 86

(1) The fiscal year 2005 program relates to the restructuring actions announced in May 2005

In addition to the fiscal year 2005 program, we recorded restructuring charges of $16 million in fiscal year 2005. These costs were primarily for severance and other employee termination costs, related to a reduction of approximately 20 salaried and 355 hourly employees, and asset impairments. These costs relate to the closure of the Sheffield, England, stabilizer bar facility, the consolidation of two facilities in Brazil and a reduction in workforce in our operations in Spain.

We recorded restructuring charges of $15 million in fiscal year 2004. These costs included severance and other employee termination costs of $10 million related to a reduction of approximately 50 salaried employees and 575 hourly employees in our LVS business, and $5 million associated with certain administrative and managerial employee termination costs.

Despite the higher sales levels, operating income in fiscal year 2005 was negatively impacted by the restructuring costs noted above and steel costs, which, net of recoveries, were approximately $90 million higher than in fiscal year 2004. Also impacting operating income in fiscal year 2005 were $14 million of charges associated with certain customer bankruptcies; $7 million of environmental remediation costs, primarily associated with a former Rockwell facility; and a $4 million gain on the sale of an automotive stamping and components manufacturing operation in the first quarter of fiscal year 2005. Retiree medical and pension costs were $16 million lower than fiscal year 2004. This is a result of amending certain retiree medical plans in fiscal year 2004, which reduced retiree medical expense by $22 million compared to fiscal year 2004.

Operating income in fiscal year 2004 includes the costs associated with the withdrawn tender offer for the outstanding shares of Dana Corporation (Dana) of $16 million (before a non-operating gain of $7 million on the sale of Dana stock owned by the company), and environmental remediation costs of $11 million (associated with a different Rockwell facility).

Selling, general and administrative expenses as a percentage of sales decreased to 4.2 percent in fiscal year 2005 from 4.8 percent in fiscal year 2004 due to reduced headcount resulting from the restructuring actions and our continued efforts to reduce selling, general and administrative spending.

Business Segments

LVS operating income was $1 million, a decrease of $117 million from operating income of $118 million in fiscal year 2004. The decrease in operating income is primarily due to the previously mentioned restructuring actions and higher steel costs in fiscal year 2005. LVS continued its restructuring efforts in fiscal year 2005 and recorded $67 million of restructuring charges

associated with facility closures and consolidations and workforce reductions compared to $10 million in the prior year. These fiscal year 2005 costs include $40 million of employee termination costs and $11 million of asset impairments related to the restructuring actions announced in May 2005. Additionally, LVS recorded $16 million of restructuring costs associated with the closure of its Sheffield, England, stabilizer bar facility, the consolidation of two facilities in Brazil and a reduction in workforce in its operations in Spain. The $16 million relates to employee termination benefits and other costs of $11 million and asset impairments of $5 million. Total headcount reductions associated with all of these actions were approximately 2,250, of which 500 were salaried employees and 1,750 were hourly employees.

LVS continued to experience narrowing margins in fiscal year 2005 due primarily to higher steel costs. LVS incurred higher net steel costs of approximately $40 million in fiscal year 2005. Also impacting operating income in fiscal year 2005, were lower value added sales volumes (non pass-through sales), $11 million of charges associated with certain customer bankruptcies and a $4 million net charge associated with a product warranty matter. LVS operating income improved by $13 million from fiscal year 2004 due to a reduction in foreign exchange loss attributable to the impact of hedging foreign exchange transactions in fiscal year 2005 that were not hedged in fiscal year 2004. LVS also recorded a $4 million gain on the sale of an automotive stamping and components manufacturing operation in the first quarter of fiscal year 2005.

CVS operating income was $193 million, an increase of $29 million from fiscal year 2004. Operating margin declined to 4.8 percent, from 5.1 percent in fiscal year 2004. The increase in operating income was largely attributable to higher sales volumes. The benefits of the higher sales volumes were partially offset by higher net steel costs of $50 million, and $19 million of restructuring costs principally associated with the reduction of approximately 225 salaried employees and 200 hourly employees. Also negatively impacting operating income was a $3 million charge associated with the bankruptcy of a European trailer customer. Retiree medical and pension costs were $18 million lower than the previous year, as a result of the amendment to certain retiree medical plans in fiscal year 2004. Fiscal year 2004 operating income included a $4 million charge in the fourth quarter associated with the settlement of a warranty matter.

Other Income Statement Items

Equity in earnings of affiliates was $28 million in fiscal year 2005, compared to $19 million in fiscal year 2004. The increase was primarily related to improved performance and higher earnings of our commercial vehicle affiliates. The increase was also partially driven by the reduction in losses associated with the dissolution of our CVS transmission joint venture with ZF Friedrichshafen in the second quarter of fiscal year 2004. We recorded equity losses of $4 million in fiscal year 2004 related to this joint venture.

Interest expense, net and other was $127 million in fiscal year 2005 compared to $107 million in fiscal year 2004. The increase in interest expense was primarily attributable to higher interest rates on our variable rate debt compared with fiscal year 2004. Also included in interest expense, net and other in fiscal year 2005 was a $4 million loss on debt extinguishment associated with the debt exchange completed in the fourth quarter of fiscal year 2005. The loss on debt extinguishment primarily consisted of the premium paid to note holders to exchange their notes. See Liquidity and Contractual Obligations for further details concerning the debt extinguishment.

Provision for income taxes was $16 million in fiscal year 2005, resulting in an effective rate of 19 percent. The effective tax rate was 27 percent in fiscal year 2004. The decline in the tax rate is principally associated with lower income levels relative to our structural tax position.

Minority interest expense was $6 million in fiscal year 2005 compared to $11 million in fiscal year 2004. Minority interests represent our minority partners share of income or loss associated with our less than 100-percent owned consolidated joint ventures. The decrease in minority interest expense in fiscal year 2005 is primarily related to our minority partners share of $9 million of restructuring costs associated with the closure of the Sheffield, England, stabilizer bar facility in our MSSC joint venture.

Income from continuing operations for fiscal year 2005 was $63 million, compared to $117 million in fiscal year 2004. The decrease was primarily attributable to the $86 million of restructuring costs and higher net steel costs of approximately $90 million, offset partially by the higher CVS sales volumes.

Loss from discontinued operations was $51 million in fiscal 2005 compared to a loss from discontinued operations of $159 million in fiscal 2004. In the fourth quarter of fiscal 2005, management concluded that it is more likely that LVA s North American businesses will be sold individually. As a result, the company evaluated fair value on an individual business basis rather than LVA North America as a whole. This resulted in a non-cash impairment charge of $43 million ($28 million after-tax) to record certain LVA North American businesses at fair value. Also impacting fiscal year 2005, were $6 million of after-tax changeover costs in LVA, associated with a new supply agreement with a significant customer, which were more than offset by

lower depreciation expense. In accordance with accounting principles generally accepted in the United States, our LVA business segment discontinued depreciating fixed assets as of September 30, 2004. Depreciation expense in fiscal year 2004 was approximately $14 million after-tax.

The fiscal year 2004 results included a non-cash goodwill impairment charge of $190 million in our LVA business and a $20 million gain on the sale of an interest in a ride control joint venture. For more information on the impairment charge see Note 3 of the Notes to Consolidated Financial Statements.

In an effort to lower fixed costs and improve profitability resulting from weakening demand in the aftermarket business, LVA recorded after-tax restructuring costs totaling $1 million and $2 million during fiscal years 2005 and 2004, respectively. We also recorded after-tax restructuring costs of $19 million related to our LVS ride control business in fiscal year 2005. These costs included $10 million of employee termination benefits and $9 million of asset impairment charges.

Also impacting loss from discontinued operations in fiscal year 2005 was the loss of approximately $6 million of income from our coil coating business as a result of the sale of this business in November 2004. This loss of net income was offset partially by a $2 million gain on the sale of this business.

The effective tax rate for discontinued operations was 30 percent in fiscal year 2005, up from a negative 9 percent in fiscal year 2004. The negative tax rate in fiscal year 2004 was primarily due to the $190 million non-cash goodwill impairment charge, for which no tax benefit was provided.

Non-Consolidated Joint Ventures

At September 30, 2006, our continuing operations had investments in 10 significant joint ventures that were not majority-owned or controlled and were accounted for under the equity method of accounting. Our investments in non-consolidated joint ventures was $133 million and $114 million at September 30, 2006 and 2005, respectively.

These strategic alliances provide for sales, product design, development and manufacturing in certain product and geographic areas. Aggregate sales of our non-consolidated joint ventures were $1,795 million, $1,488 million and $1,100 million in fiscal years 2006, 2005 and 2004, respectively.

We received cash dividends from our affiliates of $23 million, $18 million and $15 million in fiscal years 2006, 2005 and 2004, respectively.

For more information about our non-consolidated joint ventures, see Note 13 of the Notes to Consolidated Financial Statements.

Financial Condition

Capitalization

	September 30, 2006	2005
Short term debt and current maturities	$ 56	$ 136
Long term debt	1,184	1,451
Total debt	1,240	1,587
Minority interests	65	66
Shareowners equity	944	875
Total capitalization	$ 2,249	$ 2,528
Ratio of debt to capitalization	55 %	63 %

We remain committed to strong cash flow generation, the reduction of debt and regaining an investment grade credit rating. In March 2006, we issued $300 million of 4.625 percent convertible senior unsecured notes due 2026. Net proceeds from the offering, along with proceeds from the sale of certain of our LVA businesses and borrowings under our accounts receivable securitization programs, were used to purchase and extinguish $672 million of notes with maturities between 2007 and 2012. Our total debt to capitalization ratio was 55 percent at September 30, 2006, compared to 63 percent at September 30, 2005.

For fiscal year 2006, our primary source of liquidity was cash from operating activities and proceeds from the divestitures of certain businesses, supplemented by our accounts receivables securitization and factoring programs and, as required, borrowings on our revolving credit facility.

Cash Flows

	Fiscal Year Ended September 30,		
	2006	2005	2004
OPERATING CASH FLOWS			
Income (loss) from continuing operations	$(174)	$63	$117
Goodwill impairment	310		
Depreciation and amortization	172	180	179
Gain on divestitures and marketable securities	(28)	(4)	(7)
Deferred income taxes	(87)	(101)	21
Pension and retiree medical expense	142	110	130
Pension and retiree medical contributions	(114)	(164)	(212)
Restructuring costs, net of payments		44	(3)
Proceeds from termination of interest rate swaps		22	
Decrease (increase) in working capital	85	(56)	104
Changes in sale of receivables	116	(19)	(187)
Other	42	34	35
Cash flows provided by continuing operations	464	109	177
Cash flows provided by (used for) discontinued operations	(24)	(141)	42
Cash flows provided by (used for) operating activities	$440	$(32)	$219

Cash provided by operating activities was $440 million in fiscal year 2006, compared to cash used by operating activities of $32 million in fiscal year 2005. The increase in cash flow was largely driven by a reduction in working capital, including non-recourse sales of accounts receivable, and lower pension and retiree medical contributions of $50 million, partially offset by higher cash restructuring costs. In addition, in fiscal year 2005, we used approximately $110 million of cash for working capital requirements at our new joint ventures with AB Volvo and to support higher CVS volumes. In fiscal year 2005, we partially terminated certain interest rate swaps and received proceeds from these terminations, including interest received, of $22 million.

Cash used for discontinued operations was $24 million in fiscal year 2006 compared to $141 million a year ago. Lower working capital levels contributed to this decline. In addition, in fiscal year 2005, LVA ceased participating in our accounts receivable securitization program. This increased LVA s outstanding receivables by approximately $80 million during fiscal year 2005.

In fiscal year 2004, cash provided by operating activities was $219 million. Cash flow in fiscal year 2004 was favorably impacted by our fiscal calendar, which included 53 weeks in fiscal year 2004, compared to 52 weeks in fiscal year 2005. We used cash from operations and cash generated from the disposition of property, businesses and marketable securities to reduce our balances outstanding under our accounts receivable securitization and factoring programs by $187 million and our revolving credit facility by $53 million in fiscal year 2004.

	Fiscal Year Ended September 30,		
	2006	2005	2004
INVESTING CASH FLOWS			
Capital expenditures	$(150)	$(144)	$(149)
Acquisitions of businesses and investments, net of cash acquired	(6)	(31)	(3)
Proceeds from disposition of property and businesses	65	49	37
Proceeds from sale of marketable securities			18
Investment in debt defeasance trust and marketable securities	(17)		
Net cash provided by (used for) discontinued operations	218	151	(23)

CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	$110	$25	$(120)

35

Cash provided by investing activities was $110 million in fiscal year 2006, compared to $25 million in fiscal year 2005 and cash used by investing activities of $120 million in fiscal year 2004. During fiscal year 2006, we received proceeds of $39 million from the disposition of certain assets of our off-highway brakes business. We also received $26 million from the sale of various properties and machinery and equipment. These assets primarily related to closed facilities. In the third quarter of fiscal year 2006, we purchased $12 million of U.S. government securities and placed those securities into an irrevocable trust, for the sole purpose of funding payments of principal and interest through the stated maturity on $5 million principal amount of outstanding 6-3/4 percent notes due 2008 and the $6 million principal amount of outstanding 7-1/8 percent notes due 2009, in order to defease certain covenants under the associated indenture.

During fiscal year 2005, we used $31 million of cash for the acquisition of businesses, primarily the formation of two joint ventures with AB Volvo, and we received proceeds of $49 million from the disposition of certain property and businesses principally associated with the sale of our Columbus, Indiana automotive stamping and components manufacturing business.

Capital expenditures increased to $150 million in fiscal year 2006 from $144 million in fiscal year 2005. We continue to manage our capital expenditures and leverage our global supply base and the assets of our affiliate partners. As a result, capital expenditures as a percentage of sales were 1.6 percent in fiscal year 2006, flat compared to fiscal year 2005 and down from 1.9 percent in fiscal year 2004.

During fiscal year 2004, we received proceeds from the disposition of certain property and businesses of $37 million, principally from the sale of our trailer beam fabrication facility. We also received $18 million in cash from the sale of Dana stock.

Discontinued operations provided cash flows from investing activities of $218 million in fiscal year 2006, primarily related to the cash received from the sales of certain of our LVA businesses and our 39-percent equity ownership interest in Purolator India, a light vehicle aftermarket joint venture. In fiscal year 2005, discontinued operations provided investing cash flows of $151 million, primarily related to the proceeds from the sale of our coil coating business. Discontinued operations used cash of $6 million for capital expenditures in fiscal year 2006 compared to $12 million in fiscal year 2005.

In fiscal year 2004, cash used by discontinued operations was $23 million which included $54 million related to the buy-out of a lease associated with our coil coating business and capital expenditures, partially offset by $48 million of proceeds received from the sale of our interest in a joint venture.

	Fiscal Year September 30,		
	2006	2005	2004
FINANCING CASH FLOWS			
Net decrease in revolving credit facilities	$	$	$ (53)
Borrowings (payments) on accounts receivable securitization program	(72)	112	$
Proceeds from issuance of convertible notes and term loan	470		
Payments on lines of credit and other	(62)	(5)	(2)
Repayment of notes	(672)	(21)	
Net change in debt	(336)	86	(55)
Cash dividends	(28)	(28)	(28)
Debt issuance and extinguishment costs	(28)	(10)	
Proceeds from exercise of stock options	1	6	6
CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES	$ (391)	$ 54	$ (77)

Cash used for financing activities was $391 million in fiscal year 2006 compared to cash provided by financing activities of $54 million in fiscal year 2005. In the third quarter of fiscal year 2006, we replaced our $900 million revolving credit facility that was to expire in 2008 with two new senior secured credit facilities totaling $1.15 billion. The new credit facilities include a six year $170 million term loan and $980 revolving credit facility which expires in 2011. In March 2006, we issued $300 million of 4.625 percent convertible senior unsecured notes due in 2026. Net proceeds from the offering, along with proceeds from the sales of our LVA North American filters and exhaust businesses and borrowings under our accounts receivable securitization programs were used to purchase and extinguish $600 million of certain outstanding

near-term debt maturities. We incurred $28 million of costs related to these transactions. Additionally, in fiscal year 2006, we purchased, at a discount, $72 million of certain of our other fixed rate debt securities on the open market. The reduction in amounts outstanding under lines of credit and other of $62 million in fiscal year 2006 is primarily due to the payment of $35 million to extinguish a capital lease obligation.

In September 2005, we entered into a new U.S. accounts receivable securitization arrangement. Amounts outstanding under this new arrangement are reported as short-term debt in the consolidated balance sheet and related borrowings are reported as cash flows from financing activities in the consolidated statement of cash flows. At September 30, 2006 and 2005, $40 million and $112 million was outstanding under this facility, respectively.

In fiscal year 2005, we purchased, at a discount, $20 million and $1 million of our 8-3/4 percent notes and 6.8 percent notes, respectively, on the open market. In September 2005, we paid $10 million of debt issuance costs to complete an offer to exchange a new series of debt securities for $194 million of our $499 million 6.8 percent notes due in 2009, and $59 million of our $150 million 7-1/8 percent notes also due in 2009. During fiscal year 2004, we decreased amounts outstanding under our revolving credit facility by $53 million.

We paid dividends of $28 million in each of fiscal years 2006, 2005 and 2004. In each of fiscal years 2005 and 2004, proceeds of $6 million were received from the exercise of stock options.

Liquidity and Contractual Obligations

We are contractually obligated to make payments as follows (in millions):

	Total	**2007**	**2008**	**2009**	**2010-2011**	**There-after**
Total debt(1)	$1,233	$56	$24	84	$2	$1,067
Operating leases	83	23	17	14	18	11
Interest payments on long-term debt (2)	754	85	84	79	156	350
Purchase option for joint venture	23		23			
Total	$2,093	$164	$148	177	$176	$1,428

(1) Excludes fair value adjustment of notes of $8 million and unamortized debt discount of $1 million.

(2) Includes the estimated impact of our interest rate swaps.

In addition to the obligations above, in connection with the sale of our LVA North American filters business in fiscal year 2006, we agreed to indemnify the purchaser against liabilities from litigation and commercial losses in connection with specific intellectual property claims, with the maximum potential indemnity capped at $4 million for commercial losses.

We also sponsor defined benefit pension plans that cover most of our U.S. employees and certain non-U.S. employees. Our funding practice provides that annual contributions to the pension trusts will be at least equal to the minimum amounts required by ERISA in the U.S. and the actuarial recommendations or statutory requirements in other countries. Management expects funding for our retirement pension plans of approximately $134 million in fiscal year 2007.

We also sponsor retirement medical plans that cover the majority of our U.S. and certain non-U.S. employees and provide for medical payments to eligible employees and dependents upon retirement. Management expects retiree medical plan benefit payments of approximately $54 million in fiscal year 2007; $53 million in fiscal year 2008; $52 million in fiscal year 2009; $51 million in fiscal year 2010; and $50 million in fiscal year 2011.

Revolving and Other Debt In June 2006, we replaced our $900 million revolving credit facility that was to expire in 2008 with two new senior secured credit facilities totaling $1.15 billion (the new credit facilities). The new credit facilities include a $980 million revolving credit facility and a $170 million term loan maturing in 2011 and 2012, respectively. Borrowings under the new revolving credit facility are subject to interest based on quoted LIBOR rates plus a margin, and a commitment fee on undrawn amounts, both of which are based upon the company s current credit rating for the senior secured facilities. At September 30, 2006, the margin over the LIBOR rate was 150 basis points, and the commitment fee was 30 basis points. Similar to the prior revolving credit facility, the new revolving credit facility includes a $150 million limit on the issuance of letters of credit. At September 30, 2006 and 2005, approximately $25 million and $23 million of letters of credit, respectively, were issued.

The term loan is payable in quarterly installments of $0.25 million, with the remaining balance due at maturity. Borrowings under the term loan are subject to interest based on quoted LIBOR rates plus a margin. At September 30, 2006, the margin over the LIBOR rate was 175 basis points.

Borrowings under the revolving credit facility and term loan are collateralized by approximately $1.1 billion of the company s assets, primarily consisting of eligible domestic U.S. accounts receivable, inventory, plant, property, and equipment, intellectual property and the company s investment in all or a portion of certain of its wholly-owned subsidiaries.

Certain of the company s subsidiaries, as defined in the credit agreement, irrevocably and unconditionally guarantee amounts outstanding under the new credit facilities. The new credit facility requires us to maintain a total net debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio no greater than 4.25x and a minimum fixed charge coverage ratio (EBITDA less capital expenditures to interest expense) no less than 1.50x. At September 30, 2006, we were in compliance with all covenants.

We also have an arrangement with a non-consolidated joint venture that allows us to borrow funds from time to time, at LIBOR plus 50 basis points. No amounts were outstanding under this arrangement at September 30, 2006 and 2005.

Debt Securities - In fiscal year 2006, we purchased, at a discount, $69 million of our $380 million outstanding 8-3/4 percent notes and $3 million of our outstanding 6.8 percent notes on the open market.

In March 2006, we completed an offer to repurchase $600 million aggregate principal amount of our previously outstanding notes in the following amounts: $195 million of our outstanding $200 million 6.625 percent notes due in 2007; $95 million of our outstanding $100 million 6.75 percent notes due in 2008; $225 million of our outstanding $302 million 6.8 percent notes due in 2009; and $85 million of our outstanding $91 million 7.125 percent notes also due in 2009.

In the third quarter of fiscal year 2006, the company purchased $12 million of U.S. government securities and placed those securities into an irrevocable trust, for the sole purpose of funding payments of principal and interest through the stated maturity on the $5 million outstanding 6-3/4% notes due 2008 and the $6 million outstanding 7.125% notes due 2009, in order to defease certain covenants under the associated indenture.

In September 2005, we completed an offer to exchange $194 million of our previously outstanding $499 million 6.8 percent notes due in 2009, and $59 million of our previously outstanding $150 million 7-1/8 percent notes also due in 2009 for $253 million of new 8-1/8 percent notes due in 2015. Also in fiscal year 2005, we purchased, at a discount, $20 million and $1 million of our 8-3/4 percent notes and 6.8 percent notes, respectively, on the open market.

We have $150 million of debt securities remaining unissued under the shelf registration filed with the SEC in April 2001 (see Note 16 of the Notes to Consolidated Financial Statements).

Convertible Notes In March 2006, the company issued $300 million of 4.625 percent convertible senior unsecured notes due 2026 (the convertible notes). The convertible notes were sold by the company to qualified institutional buyers in a private placement exempt from the registration requirements of the Securities Act of 1933. These convertible notes were registered with the Securities and Exhange Commission under the Securities Act of 1993 on May 23, 2006. Net proceeds received by the company, after issuance costs, were $289 million. Cash interest at a rate of 4.625 percent per annum from the date of issuance through March 1, 2016 is payable semi-annually in arrears on March 1 and September 1 of each year. After March 1, 2016, the principal amount of the convertible notes will be subject to accretion at a rate that provides holders with an aggregate annual yield to maturity of 4.625 percent.

The notes are convertible into shares of the company s common stock at an initial conversion rate, subject to adjustment, equivalent to 47.6667 shares of common stock per $1,000 initial principal amount of notes, which represents an initial conversion price of approximately $20.98 per share. If converted, the accreted principal amount will be settled in cash and the remainder of the company s conversion obligation, if any, in excess of such accreted principal amount will be settled in cash, shares of common stock, or a combination thereof, at the company s election.

Holders may convert their notes at any time on or after March 1, 2024. Prior to March 1, 2024, holders may convert their notes only under the following circumstances:

during any calendar quarter, after the calendar quarter ending June 30, 2006, if the closing price of our common stock for 20 or more trading days in a perio
during the five business day period after any five consecutive trading day period in which the average trading price per $1,000 initial principal amount of n
upon the occurrence of specified corporate transactions; or
if the notes are called by us for redemption.

On or after March 1, 2016, we may redeem the convertible notes, in whole or in part, for cash at a redemption price equal to 100 percent of the accreted principal amount plus any accrued and unpaid interest. On each of March 1, 2016, 2018, 2020, 2022, and 2024, or upon certain fundamental changes, holders may require the company to purchase all or a portion of their convertible notes at a purchase price in cash equal to 100 percent of the accreted principal amount plus any accrued and unpaid interest.

Accounts Receivable Securitization and Factoring In March 2006, we entered into a new European arrangement to sell trade receivables through one of our European subsidiaries. Under the new arrangement, we can sell up to, at any point in time, 100 million ($127 million) of eligible trade receivables. The receivables under this program are sold at face value and excluded from the consolidated balance sheet. We had utilized 48 million ($61 million) of this accounts receivable securitization facility as of September 30, 2006.

In September 2005, we entered into a new $250 million U.S. accounts receivable securitization arrangement to improve financial flexibility and lower interest costs. Under the new arrangement, the company sells substantially all of the trade receivables of certain U.S. subsidiaries to ArvinMeritor Receivables Corporation (ARC), a wholly owned, consolidated special purpose subsidiary, which funds these purchases with borrowings under a loan agreement with a bank. Amounts outstanding under this agreement are collateralized by eligible receivables of ARC and are reported as short-term debt in the consolidated balance sheet. As of September 30, 2006 and 2005, we had utilized $40 million and $112 million of this accounts receivable securitization facility, respectively. If certain receivables performance-based covenants were not met, it would constitute a termination event, which, at the option of the banks, could result in termination of the accounts receivable securitization arrangement. At September 30, 2006, we were in compliance with all covenants.

In addition, several of our European subsidiaries factor eligible accounts receivable with financial institutions. The amount of factored receivables was $84 million and $23 million at September 30, 2006 and 2005, respectively. There can be no assurance that these factoring arrangements will be used or available to us in the future.

Off-Balance Sheet Arrangements

Guarantees - In December 2005, we guaranteed a third party s obligation to reimburse another party (the other party) for payment of health and prescription drug benefits to a group of retired employees. The retirees were former employees of a wholly-owned subsidiary of the company prior to it being acquired by the company. To date, the third party has met its obligations to reimburse the other party. The APBO associated with these retiree medical benefits is considered the maximum potential exposure under this guarantee, and is estimated to be approximately $25 million. No amount has been recorded for this guarantee based on the probability of our having to perform under the guarantee. Due to the nature of this guarantee it is difficult to estimate its approximate term.

We have guaranteed certain trade payable balances of one of its non-consolidated joint ventures. In the event of a default by the joint venture, we would be required to pay the guaranteed party. The maximum exposure under the guarantee is $4 million and can be terminated by the company at any time on thirty days written notice. The estimated fair value of this guarantee is not significant, and therefore, no liability is recorded.

In addition to these guarantees we have other off-balance sheet arrangements, primarily related to our European accounts receivable securitization program and letters of credit under our senior secured credit facilities. See Revolving and Other Debt and Accounts Receivable Securitization and Factoring.

Tender Offer

In the first quarter of fiscal year 2004, as a result of the company s decision to withdraw its all cash tender offer to acquire all of the outstanding shares of Dana Corporation, the company recorded a net charge of $9 million ($6 million after-tax, or $0.09 per diluted share). The pre-tax charge included $16 million in direct incremental acquisition costs, less a gain on the sale of Dana stock of $7 million.

Critical Accounting Policies

Critical accounting policies are those that are most important to the portrayal of the company s financial condition and results of operations. These policies require management s most difficult, subjective or complex judgments in the preparation of the financial statements and accompanying notes. Management makes estimates and assumptions about the effect of matters that are inherently uncertain, relating to the reporting of assets, liabilities, revenues, expenses and the disclosure of contingent assets and liabilities. Our most critical accounting policies are discussed below.

Pensions Our pension obligations are determined on an actuarial basis annually and are measured as of June 30. The U.S. plans include a qualified and non-qualified pension plan. Significant non-U.S. plans are located in the United Kingdom, Canada and Germany. The following are the significant assumptions used in the measurement of the projected benefit obligation (PBO) and net periodic pension expense:

	2006			**2005**		
	U.S.	**Non-U.S.**		**U.S.**	**Non-U.S.**	
Assumptions as of June 30						
Discount rate	6.60 %	4.75 %	5.75 %	5.30 %	4.00 %	5.00 %
Assumed return on plan assets	8.50 %	8.00 %	8.00 %	8.50 %	7.75 %	8.50 %
Rate of compensation increase	3.75 %	2.50 %	3.75 %	3.75 %	3.00 %	3.50 %

The **discount rate** is used to calculate the present value of the PBO. The rate is determined based on high-quality fixed income investments that match the duration of expected benefit payments. The company uses a portfolio of long-term corporate AA/Aa bonds that match the duration of the expected benefit payments to establish the discount rate for this assumption.

The **assumed return on plan assets** is used to determine net periodic pension expense. The rate of return assumptions are based on projected long-term market returns for the various asset classes in which the plans are invested, weighted by the target asset allocations. An incremental amount for active management, where appropriate, is included in the rate of return assumption. The return assumption is reviewed annually.

The **rate of compensation** increase represents the long-term assumption for expected increases to salaries for pay-related plans.

These assumptions reflect our historical experience and our best judgments regarding future expectations. The effects of the indicated increase and decrease in selected assumptions, assuming no changes in benefit levels and no amortization of gains or losses for the plans in 2006, are shown below (in millions):

	Effect on All Plans - June 30, 2006			
	Percentage Point Change	**Increase (Decrease) in PBO**	**Increase (Decrease) in Accumulated Other Comprehensive Loss**	**Incr**
Assumption				
Discount rate	-0.5 pts	$136	$80	$20
	+0.5 pts	(124)	(73)	(19
Assumed return on plan assets	-1.0 pts	NA	NA	12
	+1.0 pts	NA	NA	(12

NA Not Applicable

Accounting guidance applicable to pensions does not require immediate recognition of the effects of a deviation between actual and assumed experience and the revision of an estimate. This approach allows the favorable and unfavorable effects that fall within an acceptable range to be netted and disclosed as an unrecognized gain or loss in the footnotes. Based on the June 30, 2006

and 2005 measurement date, we had an unrecognized loss of $587 million and $866 million, respectively, at September 30, 2006 and 2005. A portion of this loss will be recognized into earnings in fiscal year 2007. The effect on fiscal years after 2007 will depend on the actual experience of the plans.

In recognition of the long-term nature of the liabilities of the pension plans, we have targeted an asset allocation strategy designed to promote asset growth while maintaining an acceptable level of risk over the long term. Asset-liability studies are performed periodically to validate the continued appropriateness of these asset allocation targets. The asset allocation for the U.S. plan is targeted at 50 70 percent equity securities, 25 35 percent debt securities, and 5 15 percent alternative investments. The target asset allocation ranges for the non-U.S. plans are 65 75 percent equity securities, 20 35 percent debt securities, and 0 5 percent real estate and alternative investments. The asset class mix and the percentage of securities in any asset class or market may vary as the risk/return characteristics of either individual market or asset classes vary over time.

The investment strategies for the pension plans are designed to achieve an appropriate diversification of investments as well as safety and security of the principal invested. Assets invested are allocated to certain global sub-asset categories within prescribed ranges in order to promote international diversification across security type, issuer type, investment style, industry group, and economic sector. Assets of the plans are both actively and passively managed. Policy limits are placed on the percentage of plan assets that can be invested in a security of any single issuer and minimum credit quality standards are established for debt securities. ArvinMeritor securities comprised less than one-half percent of the value of our worldwide pension assets as of September 30, 2006.

The fiscal year 2007 pension expense is estimated to be $76 million. This may vary depending upon the accuracy of our original and future assumptions.

Retiree Medical We have retirement medical plans that cover the majority of our U.S. and certain non-U.S. employees and provide for medical payments to eligible employees and dependents upon retirement. Our retiree medical obligations are measured as of June 30.

The following are the significant assumptions used in the measurement of the accumulated postretirement benefit obligation (APBO):

	2006		**2005**	
Assumptions as of June 30				
Discount rate	6.40	%	5.00	%
Health care cost trend rate (weighted average)	8.00	%	9.00	%
Ultimate health care trend rate	5.00	%	5.00	%
Year ultimate rate is reached	2011		2011	

The **discount rate** is the rate used to calculate the present value of the APBO. The rate is determined based on high-quality fixed income investments that match the duration of expected benefit payments. We have typically used the corporate AA/Aa bond rate for this assumption.

The **health care cost trend rate** represents the company s expected annual rates of change in the cost of health care benefits. The trend rate noted above represents a forward projection of health care costs as of the measurement date. Our projection for fiscal year 2007 is an increase in health care costs of 8.0 percent. For measurement purposes, the annual increase in health care costs was assumed to decrease gradually to 5.0 percent by fiscal year 2011 and remain at that level thereafter.

A one-percentage point change in the assumed health care cost trend rate for all years to, and including, the ultimate rate would have the following effects (in millions):

	2006	2005
Effect on total of service and interest cost		
1% Increase	$4	$ 3
1% Decrease	(3)	(2)
Effect on APBO		
1% Increase	55	38
1% Decrease	(47)	(35)

Fiscal year 2007 retiree medical expense is estimated to be approximately $57 million. This may vary depending upon the accuracy of our original and future assumptions.

Product Warranties Our CVS segment records product warranty costs at the time of shipment of products to customers. Liabilities for product recall campaigns are recorded at the time the company s obligation is known and can be reasonably estimated. Product warranties, including recall campaigns, not expected to be paid within one year are recorded as a non-current liability.

Our LVS segment records product warranty liabilities based on its individual customer or warranty-sharing agreements. Product warranties are recorded for known warranty issues when amounts can be reasonably estimated.

Significant factors and information used by management when estimating product warranty liabilities include:

Past claims experience;

Sales history;

Product manufacturing and industry developments; and

Recoveries from third parties.

Asbestos Maremont Corporation (Maremont) Maremont, a subsidiary of ArvinMeritor, manufactured friction products containing asbestos from 1953 through 1977, when it sold its friction product business. Arvin acquired Maremont in 1986. Maremont and many other companies are defendants in suits brought by individuals claiming personal injuries as a result of exposure to asbestos-containing products. Although Maremont has been named in these cases, very few cases allege actual injury and, in the cases where actual injury has been alleged, very few claimants have established that a Maremont product caused their injuries. Plaintiffs lawyers often sue dozens or even hundreds of defendants in individual lawsuits on behalf of hundreds or thousands of claimants, seeking damages against all named defendants irrespective of the disease or injury and irrespective of any causal connection with a particular product. For these reasons, Maremont does not consider the number of claims filed or the damages alleged to be a meaningful factor in determining its asbestos-related liability.

Prior to February 2001, Maremont participated in the Center for Claims Resolution (CCR) and shared with other CCR members in the payment of defense and indemnity costs for asbestos-related claims. The CCR handled the resolution and processing of asbestos claims on behalf of its members until February 2001, when it was reorganized and discontinued negotiating shared settlements. Since that time, Maremont has handled asbestos-related claims through its own defense counsel and has taken a more aggressive defensive approach that involves examining the merits of each asbestos-related claim.

At the end of fiscal year 2004 and through the third quarter of fiscal year 2005, Maremont established reserves for pending asbestos-related claims that reflected internal estimates of its defense and indemnity costs. These estimates were based on the history and nature of filed claims to date and Maremont s experience with historical indemnity and litigation costs, using data from actual CCR settlements, experience in resolving claims since dissolution of the CCR, and Maremont s assessment of the nature of the claims. Maremont did not accrue reserves for its potential liability for asbestos-related claims that may be asserted against it in the future, because it did not have sufficient information to make a reasonable estimate of these unknown claims.

In the fourth quarter of fiscal year 2005, Maremont worked with Bates White LLC (Bates White), a consulting firm with extensive experience estimating costs associated with asbestos litigation, to assist with determining whether it would be possible to estimate the cost of resolving pending and future asbestos-related claims that have been, and could reasonably be expected to be, filed against Maremont, as well as the cost of Maremont s share of committed but unpaid settlements entered into by the CCR. Although it is not possible to estimate the full range of costs because of various uncertainties, Bates White advised Maremont that it would be possible to determine an estimate of a reasonable forecast of the cost of resolving pending and future asbestos-related claims, based on historical data and certain assumptions with respect to events that occur in the future. We engaged Bates White to update the study as of September 30, 2006.

Bates White provided an estimate of the reasonably possible range of Maremont s obligation for asbestos personal injury claims over the next three to four years of $31 million to $44 million. After consultation with Bates White, Maremont determined that as of September 30, 2006 the most likely and probable liability for pending and future claims over the next four years is $41 million. The ultimate cost of resolving pending and future claims is estimated based on the history of claims and expenses for plaintiffs represented by law firms in jurisdictions with an established history with Maremont.

The following assumptions were made by Maremont after consultation with Bates White and are included in their study:

Pending and future claims were estimated for a four year period ending in fiscal year 2010. Maremont believes that the litigation environment will change significantly in several years, and that the reliability of estimates of future probable

expenditures in connection with asbestos-related personal injury claims declines for each year further in the future. As a result, estimating a probable liability beyond four years is difficult and uncertain;

The ultimate cost of resolving pending and future claims filed in Madison County, Illinois, a jurisdiction where a substantial amount of Maremont s claims are filed, will decline to reflect average outcomes throughout the United States;

Defense and processing costs for pending and future claims filed outside of Madison County, Illinois will be at the level consistent with Maremont s prior experience; and

The ultimate cost of resolving nonmalignant claims with plaintiffs law firms in jurisdictions without an established history with Maremont cannot be reasonably estimated. Recent changes in tort law and insufficient settlement history make estimating a liability for these nonmalignant claims difficult and uncertain.

Maremont has insurance that reimburses a substantial portion of the costs incurred defending against asbestos-related claims. The coverage also reimburses Maremont for any indemnity paid on those claims. The coverage is provided by several insurance carriers based on insurance agreements in place. Maremont has recorded a $31 million asbestos-related insurance receivable as of September 30, 2006. Certain insurance policies have been settled in cash prior to the ultimate settlement of related asbestos liabilities. Amounts received from insurance settlements generally reduce recorded insurance receivables. Receivables for policies in dispute are not recorded.

The amounts recorded for the asbestos-related reserves and recoveries from insurance companies are based upon assumptions and estimates derived from currently known facts. All such estimates of liabilities and recoveries for asbestos-related claims are subject to considerable uncertainty because such liabilities and recoveries are influenced by variables that are difficult to predict. The future litigation environment for Maremont could change significantly from its past experience, due, for example, to changes in the mix of claims filed against Maremont in terms of plaintiffs law firm, jurisdiction and disease; legislative or regulatory developments; Maremont s approach to defending claims; or payments to plaintiffs from other defendants. Estimated recoveries are influenced by coverage issues among insurers, and the continuing solvency of various insurance companies. If the assumptions with respect to the nature of pending claims, the cost to resolve claims and the amount of available insurance prove to be incorrect, the actual amount of liability for Maremont s asbestos-related claims, and the effect on the company, could differ materially from current estimates and, therefore, could have a material impact on our financial position and results of operations.

Asbestos Rockwell ArvinMeritor, along with many other companies, has also been named as a defendant in lawsuits alleging personal injury as a result of exposure to asbestos used in certain components of Rockwell products many years ago. Liability for these claims was transferred to the company at the time of the spin-off of the automotive business to Meritor from Rockwell in 1997. Currently there are thousands of claimants in lawsuits that name us, together with many other companies, as defendants. However, we do not consider the number of claims filed or the damages alleged to be a meaningful factor in determining asbestos-related liabilities. A significant portion of the claims do not identify any of Rockwell s products or specify which of the claimants, if any, were exposed to asbestos attributable to Rockwell s products, and past experience has shown that the vast majority of the claimants will never identify any of Rockwell s products. For those claimants who do show that they worked with Rockwell s products, we nevertheless believe we have meritorious defenses, in substantial part due to the integrity of the products involved, the encapsulated nature of any asbestos-containing components, and the lack of any impairing medical condition on the part of many claimants. We defend these cases vigorously. Historically, ArvinMeritor has been dismissed from the vast majority of these claims with no payment to claimants.

In the fourth quarter of fiscal year 2006, the company engaged Bates White to assist with determining whether it would be possible to estimate the cost of resolving pending and future Rockwell legacy asbestos-related claims that have been, and could reasonably be expected to be, filed against the company. Although it is not possible to estimate the full range of costs because of various uncertainties, Bates White advised the

company that it would be able to determine an estimate of probable defense costs which could be incurred to resolve pending and future Rockwell legacy asbestos-related claims. Accordingly, the company recorded a $7 million liability for defense costs associated with these claims. This estimate was based on historical data and certain assumptions with respect to events that occur in the future. Bates White was unable to determine an estimate of indemnity costs for pending or future Rockwell legacy asbestos-related claims. Bates White and management cannot reasonably estimate the ultimate liabilities for these costs, primarily because the company does not have a sufficient history of claims settlement from which to develop reliable assumptions. The uncertainties of asbestos claim litigation and resolution of the litigation with the insurance companies make it difficult to predict accurately the ultimate resolution of asbestos claims. That uncertainty is increased by the possibility of adverse rulings or new legislation affecting asbestos claim litigation or the settlement process. Subject to these uncertainties and based on the company s experience defending these asbestos claims, the company does not believe these lawsuits will have a material adverse effect on its financial condition. Rockwell was not a member of the CCR and handled its asbestos-related claims using its own litigation counsel. As a result, the company does not have any additional potential liabilities for committed CCR settlements in connection with the Rockwell-legacy cases.

Rockwell maintained insurance coverage that management believes covers indemnity and defense costs, over and above self-insurance retentions, for most of these claims. The company has initiated claims against these carriers to enforce the insurance policies. Although the status of one carrier as a financially viable entity is in question, the company expects to recover the majority of defense and indemnity costs it has incurred to date, over and above self-insured retentions, and a substantial portion of the costs for defending asbestos claims going forward. Accordingly, the company has recorded an insurance receivable related to Rockwell legacy asbestos-related liabilities of $7 million at September 30, 2006.

Environmental We record liabilities for environmental issues in the accounting period in which our responsibility and remediation plans are established and the cost can be reasonably estimated. At environmental sites in which more than one potentially responsible party has been identified, we record a liability for our allocable share of costs related to our involvement with the site, as well as an allocable share of costs related to insolvent parties or unidentified shares. At environmental sites in which we are the only potentially responsible party, a liability is recorded for the total estimated costs of remediation before consideration of recovery from insurers or other third parties. The ultimate cost with respect to our environmental obligations could significantly exceed the costs we have recorded as liabilities. Significant factors considered by management when estimating environmental reserves include:

- Evaluations of current law and existing technologies;
- The outcome of discussions with regulatory agencies;
- Physical and scientific data at the site;
- Government regulations and legal standards; and
- Proposed remedies and technologies.

Goodwill Goodwill is reviewed for impairment annually or more frequently if certain indicators arise. If business conditions or other factors cause the profitability and cash flows of a reporting unit to decline, we may be required to record impairment charges for goodwill at that time. The goodwill impairment review is a two-step process. Step one consists of a comparison of the fair value of a reporting unit with its carrying amount. An impairment loss may be recognized if the review indicates that the carrying value of a reporting unit exceeds its fair value. Estimates of fair value are primarily determined by using discounted cash flows and market multiples on earnings. If the carrying amount of a reporting unit exceeds its fair value, step two requires the fair value of the reporting unit to be allocated to the underlying assets and liabilities of that reporting unit, resulting in an implied fair value of goodwill. If the carrying amount of the goodwill of the reporting unit exceeds the implied fair value, an impairment charge is recorded equal to the excess.

The impairment review is highly judgmental and involves the use of significant estimates and assumption. These estimates and assumptions have a significant impact on the amount of any impairment charge recorded. Discounted cash flow methods are dependent upon assumption of future sales trends, market conditions and cash flows of each reporting unit over several years. Actual cash flows in the future may differ significantly from those previously forecasted. Other significant assumptions include growth rates and the discount rate applicable to future cash flows.

Impairment of Long-Lived Assets Long-lived assets, excluding goodwill, to be held and used are reviewed for impairment whenever adverse events or changes in circumstances indicate a possible impairment. An impairment loss is recognized when the long-lived assets carrying value exceeds the fair value. If business conditions or other factors cause the profitability and cash flows to decline, we may be required to record impairment charges at that time. Long-lived assets held for sale are recorded at the lower of their carrying amount or fair value less cost to sell. Significant judgments and estimates used by management when evaluating long-lived assets for impairment include:

- An assessment as to whether an adverse event or circumstance has triggered the need for an impairment review; and

- Undiscounted future cash flows generated by the asset.

Income Taxes Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. If it is more likely than not that the deferred tax asset will be realized, no valuation allowance is recorded. Management judgment is required in determining the company s provision for income taxes, deferred tax assets and liabilities and the valuation allowance recorded against the company s net deferred tax assets. The valuation allowance would need to be adjusted in the event future taxable income is materially different than amounts estimated. Significant judgments, estimates and factors considered by management in its determination of the probability of the realization of deferred tax assets include:

Historical operating results;

Expectations of future earnings;

Tax planning strategies; and

The extended period of time over which retirement medical and pension liabilities will be paid.

As of September 30, 2006, the company had approximately $457 million in U.S. net deferred tax assets. These deferred tax assets include net operating loss carryovers that can be used to offset taxable income in future periods and reduce income taxes payable in those future periods. However, many of these deferred taxes will expire if they are not utilized within certain time periods. It is possible that some or all of these deferred tax assets could ultimately expire unused. Risk factors include (a) a more severe than expected downturn in the fiscal year 2007 outlook for the company s CVS segment, which has significant U.S. operations, (b) higher than planned volume or price reductions from the company s key customers and (c) higher than planned material cost increases.

These risk factors are offset by the following strategic initiatives: (a) the company has undertaken numerous restructuring initiatives in 2006 which are expected to result in significant savings in future periods, (b) the commercial vehicle market in the United States is expected to recover in 2008 and 2009 significantly benefiting the company and (c) the company has announced that it is embarking on a major cost redcution and value creation program that is expected to generate significant improvements in earnings in future periods.

The expiration periods for $556 million of deferred tax assets related to net operating losses and tax credit carryforwards are as follows: $30 million between fiscal years 2007 and 2011; $53 million between fiscal years 2012 and 2021; $242 million between fiscal years 2022 and 2026; and $231 million can be carriedfoward indefinitely. The company has provided valuation allowances on these deferred tax assets of approximately $22 million, $30 million, $8 million and $123 million, respectively.

New Accounting Pronouncements

New accounting standards to be implemented:

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN 48 provides criteria for subsequently recognizing, derecognizing and measuring changes in uncertain tax positions and requires expanded disclosures with respect to the uncertainty of income taxes. The accounting provisions of FIN 48 will be effective for the company beginning October 1, 2007 with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. We are in the process of determining the effect the adoption of FIN 48 will have on our consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157 (SFAS 157), Fair Value Measurements which provides a definition of fair value establishes a framework for measuring fair value and requires expanded disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those years. The provisions of SFAS 157 will be applied prospectively.

In September 2006, the FASB issued SFAS No. 158 (SFAS 158), Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R) . This statement requires an entity to recognize the funded status of its

defined benefit pension plans and other postretirement benefit plans, such as a retiree health care plan, on the balance sheet and to recognize changes in the funded status, that arise during the period but are not recognized as components of net periodic benefit cost, within other comprehensive income, net of income taxes. SFAS 158 also requires measurement of the funded status of the plans as of the balance sheet date. SFAS 158 is effective for recognition of the funded status of the plans for fiscal years ending after December 15, 2006 and is effective for the measurement date provisions for fiscal years ending after December 15, 2008. The impact of this statement will be dependent upon our June 30, 2007 actuarial valuation and changes in assumptions compared to the current year s valuation. However, if this standard had been effective for the year ended September 30, 2006, the impact would have been a reduction to shareowners equity, net of tax, of approximately $300 million.

In September 2006, the SEC issued Staff Accounting Bulletin (SAB) No. 108, Quantifying Financial Misstatements , which expresses the Staff s views regarding the process of quantifying financial statement misstatements. Registrants are required to quantify the impact of correcting all misstatements, including both the carryover and reversing effects of prior year misstatements, on the current year financial statements. The financial statements would require adjustment when either approach results in quantifying a misstatement that is material, after considering all relevant quantitative and qualitative factors. SAB 108 is effective for financial

statements covering the first fiscal year ending after November 15, 2006. We are in the process of determining the effect, if any, SAB No. 108 will have on our consolidated financial statements.

New accounting standards implemented:

In March 2005, the FASB issued Interpretation No. 47 (FIN 47), Accounting for Conditional Asset Retirement Obligations, an interpretation of SFAS No. 143, Accounting for Asset Retirement Obligations. FIN 47 clarifies the term conditional asset retirement obligation as used in SFAS No. 143 and provides clarification with respect to the timing of liability recognition for such obligations. Conditional asset retirement obligations represent a legal obligation to perform asset retirement activities in which the timing and/or method of settlement are conditional on a future event. FIN 47 requires an entity to recognize a liability for the fair value of a conditional asset retirement obligation when incurred if the liability s fair value can be reasonably estimated. We adopted FIN 47 in the fourth quarter of fiscal year 2006. The adoption of FIN 47 did not have a material impact on the company s results of operations or financial position.

In December 2004, the FASB issued SFAS No. 123(R), *Share-Based Payment,* which requires compensation costs related to share-based payment transactions to be recognized in the financial statements. This statement also establishes fair value as the measurement objective for share-based payment transactions with employees. The company began expensing the fair value of stock options in fiscal year 2002. The company adopted the provisions of SFAS No. 123(R) in the first quarter of fiscal year 2006, which resulted primarily in changing the company s method of accounting for retirement eligible employees and estimating forfeitures for unvested stock based compensation awards. Subsequent to adoption, the company began recognizing compensation expense associated with stock grants to retirement eligible employees during the year granted. Prior to adoption, the company expensed stock compensation granted to retirement eligible employees ratably over the respective vesting period. Also upon adoption the company reclassified amounts recorded in unearned compensation (a contra-equity account) to additional paid-in-capital in the consolidated balance sheet. The adoption of SFAS No. 123(R) did not have a material impact on the company s results of operations or financial position.

In December 2004, the FASB issued Staff Position (FSP) FAS 109-2, *Accounting and Disclosure Guidance for the Foreign Repatriation Provision within the American Jobs Creation Act of 2004.* The American Jobs Creation Act of 2004 (the Act) creates a temporary incentive for U.S. corporations to repatriate foreign subsidiary earnings by providing an elective 85 percent dividends received deductions for certain dividends from controlled foreign corporations. The FSP addresses whether a company should be allowed additional time beyond the financial reporting period in which the Act was enacted, to evaluate the effects of the Act on the company s plan for reinvestment or repatriation of foreign earnings for purposes of applying SFAS No. 109. Prior to the fourth quarter of the fiscal year ended September 30, 2006, the company was evaluating the repatriation provisions of the Act and could not reasonably estimate a range of the income tax effects of such repatriation. There were numerous factors that were not controllable by the company that made it difficult for us to determine whether to take advantage of the Act and if so determined, to estimate the range of the income tax effects prior to the fourth quarter of fiscal year 2006. These factors included approvals by government bodies and employee groups. In the fourth quarter of fiscal year 2006 we repatriated approximately $152 million in dividends subject to the elective 85 percent dividend received deduction and recorded a corresponding tax benefit of $37 million related to the reversal of previously provided U.S. deferred tax liability on these unremitted foreign subsidiary earnings. The dividend was paid in September 2006.

International Operations

Approximately 48 percent of the company s total assets, excluding assets of discontinued operations, as of September 30, 2006, and 50 percent of fiscal 2006 sales from continuing operations were outside North America. Management believes that international operations have significantly benefited the financial performance of the company. However, our international operations are subject to a number of risks inherent in operating abroad. There can be no assurance that these risks will not have a material adverse impact on our ability to increase or maintain our foreign sales or on our financial condition or results of operations.

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Item 7A. ***Quantitative and Qualitative Disclosures About Market Risk.***

We are exposed to global market risks, including foreign currency exchange rate risk related to our transactions denominated in currencies other than the U.S. dollar and interest rate risk associated with our debt.

We use foreign currency forward contracts to manage the exposures arising from foreign currency exchange risk. Gains and losses on the underlying foreign currency exposures are partially offset with gains and losses on the foreign currency forward contracts. Under this program, we have designated the foreign currency contracts (the contracts) as cash flow hedges of underlying foreign currency forecasted purchases and sales. The effective portion of changes in the fair value of the contracts is recorded in Accumulated Other Comprehensive Income (AOCI) in the statement of shareowners equity and is recognized in operating income when the underlying forecasted transaction impacts earnings. The contracts generally mature within 12 months. Prior to this program, we used foreign exchange contracts to offset the effect of exchange rate fluctuations on foreign currency denominated payables and receivables but did not designate these contracts as hedges for accounting purposes. These contracts were generally of short duration (less than three months). It is difficult to predict the impact the euro and other currencies will have on our sales and operating income.

We also use interest rate swaps to manage the proportion of variable rate debt to fixed rate debt. It is our policy not to enter into derivative instruments for speculative purposes, and therefore, we hold no derivative instruments for trading purposes.

Sensitivity Analysis: We use sensitivity models to calculate the fair value and cash flow impact that a hypothetical change in market currency rates and interest rates would have on derivative and debt instruments. Actual gains or losses in the future may differ significantly from that analysis, however, based on changes in the timing and amount of interest rate and foreign currency exchange rate movements and the company s actual exposures.

The results of the sensitivity analysis are as follows (in millions):

Market Risk	Assuming a 10% Increase in Rates	Assuming a 10% Decrease in Rates	Favorable / (Unfavorable) Impact on
Foreign Currency Sensitivity:			
Forward contracts (1)	$ 11.0	$ (11.0)	Fair Value
Foreign currency denominated debt	$ 1.8	$ (1.8)	Fair Value
Interest Rate Sensitivity:			
Debt - fixed rate	$ (42.7)	$ 46.0	Fair Value
Debt - variable rate	$ (2.9)	$ 2.9	Cash Flow
Interest rate swaps (pay variable, receive fixed)	$ (2.1)	$ 2.1	Fair Value

(1) Includes only the risk related to the derivative instruments that serve as hedges and does not include the risk related to the underlying hedged item or on other operating transactions. The analyses assume overall derivative instruments and debt levels remain unchanged for each hypothetical scenario.

Item 8. ***Financial Statements and Supplementary Data.***

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareowners of ArvinMeritor, Inc.

Troy, Michigan

We have audited the accompanying consolidated balance sheets of ArvinMeritor, Inc. (the Company) as of September 30, 2006 and 2005, and the related consolidated statements of operations, cash flows and shareowners equity for each of the three years in the period ended September 30, 2006. Our audits also included the financial statement schedule listed in the Index at Item 15(a)(2). These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of ArvinMeritor, Inc. as of September 30, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2006, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of September 30, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated November 17, 2006 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

DELOITTE & TOUCHE LLP

Detroit, Michigan

November 17, 2006

ARVINMERITOR, INC.

CONSOLIDATED STATEMENT OF OPERATIONS

(In millions, except per share amounts)

	Year Ended September 30, 2006	2005	2004
Sales	$ 9,195	$ 8,873	$ 7,887
Cost of sales	(8,607)	(8,214)	(7,208)
GROSS MARGIN	588	659	679
Selling, general and administrative	(380)	(376)	(382)
Goodwill impairment	(310)		
Restructuring costs	(37)	(86)	(15)
Other income (expense)	20	(13)	(27)
OPERATING INCOME (LOSS)	(119)	184	255
Equity in earnings of affiliates	36	28	19
Gain on sale of marketable securities			7
Interest expense, net and other	(133)	(127)	(107)
INCOME (LOSS) BEFORE INCOME TAXES	(216)	85	174
Benefit (provision) for income taxes	56	(16)	(46)
Minority interest	(14)	(6)	(11)
INCOME (LOSS) FROM CONTINUING OPERATIONS	(174)	63	117
LOSS FROM DISCONTINUED OPERATIONS, net of tax	(1)	(51)	(159)
NET INCOME (LOSS)	$ (175)	$ 12	$ (42)
BASIC EARNINGS (LOSS) PER SHARE			
Continuing operations	(2.51)	$ 0.92	$ 1.74
Discontinued operations	(0.01)	(0.75)	(2.36)
Basic earnings (loss) per share	$ (2.52)	$ 0.17	$ (0.62)
DILUTED EARNINGS (LOSS) PER SHARE			
Continuing operations	(2.51)	$ 0.90	$ 1.71
Discontinued operations	(0.01)	(0.73)	(2.32)
Diluted earnings (loss) per share	$ (2.52)	$ 0.17	$ (0.61)
Basic average common shares outstanding	69.3	68.5	67.4
Diluted average common shares outstanding	69.3	69.9	68.6

See Notes to Consolidated Financial Statements. Fiscal year 2005 and 2004 amounts have been restated for discontinued operations.

ARVINMERITOR, INC.

CONSOLIDATED BALANCE SHEET

(In millions)

	September 30, 2006	2005
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$350	$187
Receivables, net	1,645	1,669
Inventories	596	555
Other current assets	295	256
Assets of discontinued operations	207	491
TOTAL CURRENT ASSETS	3,093	3,158
NET PROPERTY	988	1,024
GOODWILL	503	801
OTHER ASSETS	929	887
TOTAL ASSETS	$5,513	$5,870
LIABILITIES AND SHAREOWNERS EQUITY		
CURRENT LIABILITIES:		
Short-term debt	$56	$136
Accounts payable	1,649	1,490
Other current liabilities	741	675
Liabilities of discontinued operations	103	214
TOTAL CURRENT LIABILITIES	2,549	2,515
LONG-TERM DEBT	1,184	1,451
RETIREMENT BENEFITS	507	754
OTHER LIABILITIES	264	209
MINORITY INTERESTS	65	66
SHAREOWNERS EQUITY:		
Common stock (2006, 71.0 shares issued and 70.6 outstanding; 2005, 71.0 shares issued and 70.3 outstanding)	71	71
Additional paid-in capital	587	580
Retained earnings	376	579
Treasury stock (2006, 0.4 shares; 2005, 0.7 shares)	(11)	(10)
Unearned compensation		(13)
Accumulated other comprehensive loss	(79)	(332)
TOTAL SHAREOWNERS EQUITY	944	875
TOTAL LIABILITIES AND SHAREOWNERS EQUITY	$5,513	$5,870

See Notes to Consolidated Financial Statements. Fiscal year 2005 amounts have been restated for discontinued operations.

ARVINMERITOR, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(In millions)

	Year Ended September 30,		
	2006	**2005**	**2004**
OPERATING ACTIVITIES			
Income (loss) from continuing operations	$ (174)	$ 63	$ 117
Adjustments to income (loss) from continuing operations to arrive at cash provided by (used for) operating activities:			
Goodwill impairment	310		
Depreciation and amortization	172	180	179
Gain on divestitures and marketable securities	(28)	(4)	(7)
Restructuring costs, net of payments		44	(3)
Loss on debt extinguishment, net	6	4	
Deferred income tax	(87)	(101)	21
Equity in earnings of affiliates, net of dividends	(13)	(10)	(4)
Stock compensation expense	17	24	16
Provision for doubtful accounts	8	19	19
Pension and retiree medical expense	142	110	130
Pension and retiree medical contributions	(114)	(164)	(212)
Proceeds from terminations of interest rate swaps		22	
Changes in receivable securitization and factoring	116	(19)	(187)
Changes in assets and liabilities, excluding effects of acquisitions, divestitures and foreign currency adjustments and discontinued operations:			
Receivables	(39)	(205)	(90)
Inventories	(32)	(27)	(63)
Accounts payable	131	155	217
Other current assets and liabilities	25	21	40
Other assets and liabilities	24	(3)	4
Operating cash flows provided by continuing operations	464	109	177
Operating cash flows provided by (used for) discontinued operations	(24)	(141)	42
CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	440	(32)	219
INVESTING ACTIVITIES			
Capital expenditures	(150)	(144)	(149)
Acquisitions of businesses and investments, net of cash acquired	(6)	(31)	(3)
Proceeds from disposition of property and businesses	65	49	37
Investment in debt defeasance trust and marketable securities	(17)		
Proceeds from sale of marketable securities			18
Net investing cash flows provided by (used for) discontinued operations	218	151	(23)
CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	110	25	(120)
FINANCING ACTIVITIES			
Net decrease in revolving credit facilities			(53)
Net change in accounts receivable securitization program	(72)	112	
Proceeds from issuance of notes and term loan	470		
Repayment of notes	(672)	(21)	
Payments on lines of credit and other	(62)	(5)	(2)
Net change in debt	(336)	86	(55)
Debt issuance and extinguishment costs	(28)	(10)	
Cash dividends	(28)	(28)	(28)
Proceeds from exercise of stock options	1	6	6
CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES	(391)	54	(77)