WATERS CORP /DE/
Form 10-K
March 01, 2007

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2006

or

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

Commission File Number: 01-14010

Waters Corporation
(Exact name of registrant as specified in its charter)

Delaware	**13-3668640**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

34 Maple Street
Milford, Massachusetts 01757
(Address, including zip code, of principal executive offices)

Registrant s telephone number, including area code: (508) 478-2000

Securities registered pursuant to Section 12(b) of the Act:	Common Stock, par value $0.01 per share New York Stock Exchange, Inc.
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 þ No o

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

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 þ No o

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. þ

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

State the aggregate market value of the registrant s common stock held by non-affiliates of the registrant as of July 1, 2006: $4,545,672,000.

Indicate the number of shares outstanding of the registrant s common stock as of February 23, 2007: 101,531,747

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the 2007 Annual Meeting of Stockholders are incorporated by reference in Part III, including, specifically, the Compensation Committee Report to be included in that proxy statement.

WATERS CORPORATION AND SUBSIDIARIES

ANNUAL REPORT ON FORM 10-K

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EX-31.2 Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

EX-32.1 Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

EX-32.2 Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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PART I

Item 1: *Business*

General

Waters Corporation (Waters or the Company), an analytical instrument manufacturer, designs, manufactures, sells and services, through its Waters Division, high performance liquid chromatography (HPLC), ultra performance liquid chromatography (UPLC and together with HPLC, herein referred to as LC) and mass spectrometry (MS) instrument systems and support products, including chromatography columns, other consumable products and comprehensive post-warranty service plans. These systems are complementary products that can be integrated together and used along with other analytical instruments. Through its TA Division (TA), the Company designs, manufactures, sells and services thermal analysis and rheometry instruments which are used primarily in predicting the suitability of polymers and viscous liquids for various industrial, consumer goods and health care products. The Company is also a developer and supplier of software based products that interface with the Company s instruments as well as other instrument manufacturers instruments.

The Company s products are used by pharmaceutical, life science, biochemical, industrial, academic and government customers working in research and development, quality assurance and other laboratory applications. The Company s LC and MS instruments are utilized in this broad range of industries to detect, identify, monitor and measure the chemical, physical and biological composition of materials as well as to purify a full range of compounds. These instruments are used in drug discovery and development, including clinical trial testing, the analysis of proteins in disease processes (known as proteomics), food safety analyses and environmental testing. The Company s thermal analysis and rheometry instruments are used in predicting the suitability of fine chemicals and polymers for uses in various industrial, consumer goods and health care products.

The Company typically experiences a seasonal increase in sales in its fourth quarter, as a result of purchasing habits for capital goods by customers who tend to exhaust their spending budgets by calendar year-end.

Waters is a holding company that owns all of the outstanding common stock of Waters Technologies Corporation, its operating subsidiary. Waters became a publicly traded company with its initial public offering (IPO) in November 1995. Since the IPO, the Company has added two significant and complementary technologies to its range of products with the acquisitions of TA Instruments in May 1996 and Micromass Limited (Micromass) in September 1997.

Business Segments

The Company s business activities, for which discrete financial information is available, are regularly reviewed and evaluated by the Chief Executive Officer. As a result of this evaluation, the Company determined that it has two operating segments: Waters Division and TA Division. As indicated above, the Company operates in the analytical instruments industry, manufacturing, distributing and servicing products in three complementary technologies: LC and MS instruments, columns and other consumables, and thermal analysis and rheometry instruments. The Company s two operating segments, Waters Division and TA, have similar economic characteristics, product processes, products and services, types and classes of customers, methods of distribution, and regulatory environments. Because of these similarities, the two segments have been aggregated into one reporting segment for financial statement purposes.

Information concerning revenues and long-lived assets attributable to each of the Company s geographic areas is set forth in Note 17 of Notes to the Consolidated Financial Statements, which is incorporated herein by reference.

WATERS DIVISION

High Performance and Ultra Performance Liquid Chromatography

Developed in the 1950 s, HPLC is the standard technique used to identify and analyze the constituent components of a variety of chemicals and other materials. The Company believes that HPLC s performance capabilities enable it to separate and identify approximately 80% of all known chemicals and materials. As a result, HPLC is used to

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analyze substances in a wide variety of industries for research and development purposes, quality control and process engineering applications.

The most significant end-use markets for HPLC are those served by the pharmaceutical and life science industries. In these markets, HPLC is used extensively to identify new drugs, to develop manufacturing methods, and to assure the potency and purity of new pharmaceuticals. HPLC is also used in a variety of other applications, such as analyses of foods and beverages for nutritional labeling and compliance with safety regulations, the testing of water and air purity within the environmental testing industry, as well as applications in other industries, such as chemical and consumer products. HPLC is also used by universities, research institutions and government agencies, and in many instances, the United States Food and Drug Administration (FDA) and the United States Environmental Protection Agency (EPA) and their international counterparts who mandate testing that requires HPLC instrumentation.

Traditionally, a typical HPLC system has consisted of five basic components: solvent delivery system, sample injector, separation column, detector and data acquisition unit. The solvent delivery system pumps the solvent through the HPLC system, while the sample injector introduces the sample into the solvent flow. The chromatography column then separates the sample into its components for analysis by the detector, which measures the presence and amount of the constituents. The data acquisition unit, usually referred to as the instrument s software or data system, then records and stores the information from the detector.

In March 2004, Waters introduced a novel technology that the Company described as Ultra-Performance Liquid Chromatography that utilizes a packing material with small, uniform diameter particles and a specialized instrument, the ACQUITY UPLC®, to accommodate the increased pressure and narrow chromatographic bands that are generated by these small particles. By using the ACQUITY UPLC, researchers and analysts are able to achieve more comprehensive chemical separations and faster analysis times in comparison with many analyses performed by HPLC. In addition, in using ACQUITY UPLC, researchers have the potential to extend the range of application beyond that of HPLC, enabling the uncovering of new levels of scientific information. Though it offers significant performance advantages, ACQUITY UPLC is compatible with the Company s software products and the general operating protocols of HPLC. For these reasons, the Company s customers and field sales and support organizations are well positioned to utilize this new technology and instrument. The Company began shipping the ACQUITY UPLC in the third quarter of 2004. During 2006 and 2005, the Company experienced growth in the instrument systems product line primarily from the sales of the ACQUITY UPLC.

The primary consumable products for LC are chromatography columns. These columns are packed with separation media used in the LC testing process and are replaced at regular intervals. The chromatography column contains one of several types of packing, typically stationary phase particles made from silica. As the sample flows through the column, it is separated into its constituent components.

Waters HPLC columns can be used on Waters-branded, as well as competitors , LC systems. The Company believes that it is one of the few suppliers in the world that processes silica, packs columns and distributes its own products. In doing so, the Company believes it can better ensure product consistency, a key attribute for its customers in quality control laboratories, and react quickly to new customer requirements. At this time, the Company believes that its ACQUITY UPLC lines of columns are used nearly exclusively on its ACQUITY UPLC instrument and, furthermore, that its ACQUITY UPLC instrument will primarily use ACQUITY UPLC columns. In 2006 and 2005, excluding the small impact from acquisitions mentioned below, the Company experienced growth in its LC chromatography column and sample preparation businesses, especially in the XBridge™, SunFire™ and ACQUITY UPLC columns, as well as in Oasis® sample preparation cartridges.

In February 2006, the Company acquired the net assets of the food safety business of VICAM Limited Partnership (VICAM) for $13.8 million in cash. VICAM is a leading provider of tests to identify and quantify toxins in various

agricultural commodities. The Company s test kits provide reliable, quantitative detection of particular toxins through the choice of flurometer or HPLC. In December 2006, the Company acquired all of the outstanding capital stock of Environmental Resources Associates, Inc. (ERA), a provider of environmental testing products for quality control, proficiency testing and specialty calibration chemicals used in environmental laboratories, for $62.5 million in cash and the assumption of $3.8 million of debt. ERA also provides product

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support services required to help laboratories with their federal and state mandated accreditation requirements or with quality control over critical pharmaceutical analysis.

Based upon reports from independent marketing research firms and publicly disclosed sales figures from competitors, the Company believes that it is one of the world s largest manufacturers and distributors of LC instruments, chromatography columns and other consumables and related services. The Company also believes that it has the leading LC market share in the United States, Europe and Asia and believes it has a leading market share position in Japan.

Waters manufactures LC instruments that are offered in configurations that allow for varying degrees of automation, from component configured systems for academic research applications to fully automated Alliance® 2795 systems for high speed screening, and with a variety of detection technologies, from ultra-violet (UV) absorbance to MS, optimized for certain analyses. The Company also manufactures tailored LC systems for the analysis of biologics as well as an LC detector utilizing evaporative light scattering technology to expand the usage of LC to compounds that are not amenable to UV absorbance detection.

The servicing and support of LC and MS instruments and accessories is an important source of revenue for the Waters Division. These revenues are derived primarily through the sale of support plans, demand service, customer training and performance validation services. Support plans most typically involve scheduled instrument maintenance, a commitment to supply software and firmware upgrades and an agreement to promptly repair a non-functioning instrument in return for a fee described in a multi-year contract that is priced according to the configuration of the instrument.

Mass Spectrometry

Mass spectrometry is a powerful analytical technique that is used to identify unknown compounds, to quantify known materials, and to elucidate the structural and chemical properties of molecules by measuring the masses of individual molecules that have been converted into ions.

The Company believes it is a market leader in the development, manufacture, sale and distribution of MS instruments. These instruments can be integrated and used along with other complementary analytical instruments and systems such as LC, chemical electrophoresis, chemical electrophoresis chromatography and gas chromatography. A wide variety of instrumental designs fall within the overall category of MS instrumentation, including devices that incorporate quadrupole, ion trap, time of flight (Tof) and classical magnetic sector technologies. Furthermore, these technologies are often used in tandem to maximize the efficacy of certain experiments.

Currently, the Company offers and provides service, support and training for a wide range of MS instruments utilizing various combinations of quadrupole, Tof and magnetic sector designs. These instruments are used in drug discovery and development, as well as for environmental testing. The majority of mass spectrometers sold by the Company are designed to utilize an LC system as the sample introduction device. These products supply a diverse market with a strong emphasis on the life science, pharmaceutical, biomedical, clinical and environmental market segments worldwide. Service sales, included in Waters Division total service sales, are primarily related to the sale of parts and labor associated with instrument repair and routine maintenance.

The mass spectrometer is an increasingly important detection device for LC. The Company s smaller sized mass spectrometers (such as the SQD and the TQD) are often referred to as LC detectors and are either sold as part of an LC system or as an LC upgrade. Large quadrupole systems, such as the Waters Quattro micro™ and Quattro Premier™ XE instruments, are used primarily for experiments performed for late stage drug development, including clinical trial testing, and Q-Tof instruments, such as the Company s Q-Tof micro™ and Q-Tof Premier™ instruments, are often used

to analyze the role of proteins in disease processes, an application sometimes referred to as proteomics . In late 2006, the Company also introduced a new Tandem Quadrupole device, the TQD, and a new hybrid quadrupole time of flight technology system, the Synapt[tm] HDMS. The Synapt HDMS system integrates ion mobility technology within a Q-Tof geometry instrument configuration and uniquely allows researchers to glean molecular shape information, a novel capability for a mass spectrometry instrument. The introduction of these new products has augmented the recent growth of the MS instrument systems. In 2005, the Company introduced a new enhanced tandem quadrupole instrument, the Quattro Premier XE and the LCT Premier[tm]. The LCT Premier is

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an LC, electrospray-Tof instrument designed to deliver a higher level of mass accuracy and the ability for more precise quantitative analysis. In 2004, the Company introduced a new Q-Tof configuration mass spectrometry system, the Q-Tof Premier to replace its Q-Tof Ultima® line of systems and offer a higher level of instrument performance to its customers. The Q-Tof Premier is a tandem mass spectrometry system developed to provide increased levels of sensitivity and specificity to customers involved in challenging analyses such as those often encountered in proteomics and metabolite profiling experiments. The Company began shipping the Q-Tof Premier in the fourth quarter of 2004. The Q-Tof Premier is compatible and often purchased with a specialized ACQUITY UPLC as an inlet, a device to efficiently introduce a separated sample into the mass spectrometer.

LC-MS

LC and MS are instrumental technologies often embodied within an analytical system tailored for either a dedicated class of analyses or as a general purpose analytical device. An increasing percentage of the Company s customers are purchasing LC and MS components simultaneously and it is becoming common for LC and MS instrumentation to be used within the same laboratory and be operated by the same user. The descriptions of LC and MS above reflect the historical segmentation of these analytical technologies and the historical categorization of their respective practitioners. Increasingly in today s instrument market, this segmentation and categorization is becoming obsolete as a high percentage of instruments used in the laboratory embody both LC and MS technologies as part of a single device. In response to this development and to further promote the high utilization of these hybrid instruments, the Company has organized its Waters Division to develop, manufacture, sell, service and support integrated LC-MS systems.

TA DIVISION

Thermal Analysis

Thermal analysis measures the physical characteristics of materials as a function of temperature. Changes in temperature affect several characteristics of materials such as their physical state, weight, dimension and mechanical and electrical properties, which may be measured by one or more thermal analysis techniques. Consequently, thermal analysis techniques are widely used in the development, production and characterization of materials in various industries such as plastics, chemicals, automobiles, pharmaceuticals and electronics.

Rheometry instruments complement thermal analyzers in characterizing materials. Rheometry characterizes the flow properties of materials and measures their viscosity, elasticity and deformation under different types of loading or conditions. The information obtained under such conditions provides insight to a material s behavior during manufacturing, transport, usage and storage.

Thermal analysis and rheometry instruments are heavily used in material testing laboratories and, in many cases, provide information useful in predicting the suitability of polymers and viscous liquids for various industrial, consumer goods and health care products. As with systems offered through the Waters Division, a range of instrumental configurations are available with increasing levels of sample handling and information processing automation. In addition, systems and accompanying software packages can be tailored for specific applications. For example, the Q-Series™ family of differential scanning calorimeters includes a range of instruments from basic dedicated analyzers to more expensive systems that can accommodate robotic sample handlers and a variety of sample cells and temperature control features for analyzing a broad range of materials. In 2006, TA introduced four new differential scanning calorimeters. During 2005, TA introduced a new thermogravimetric analyzer (TGA), the Q5000IR TGA, and a new AR-G2 rheometer. The introduction of these new products significantly helped grow the TA business in 2006 and 2005.

In August 2006, the Company acquired all of the outstanding capital stock of Thermometric AB (Thermometrics), a manufacturer of high performance microcalorimeters, for $2.5 million in cash and the assumption of $1.2 million in debt. Thermometrics flagship product, the TAM III, is a modular calorimeter that employs proprietary technology to deliver unparalleled calorimetric sensitivity and temperature stability. It is routinely used to characterize materials, and their interactions, in the fields of pharmaceuticals, life and materials sciences. The TAM III systems complement TA s industry leading Q-Series differential scanning calorimeter product line and enhances TA s position as the world s leading supplier of thermal analysis instrumentation.

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The Company sells, supports and services these product offerings through TA, headquartered in New Castle, Delaware. TA operates independently from the Waters Division though several of its overseas offices are situated in Waters facilities. TA has dedicated field sales and service operations. Service sales are primarily derived from the sale of replacement parts and from billed labor fees associated with the repair, maintenance and upgrade of installed systems.

Customers

The Company has a broad and diversified customer base that includes pharmaceutical accounts, other industrial accounts, universities and government agencies. The pharmaceutical segment represents the Company s largest sector and includes multi-national pharmaceutical companies, generic drug manufacturers and biotechnology companies. The Company s other industrial customers include chemical manufacturers, polymer manufacturers, food and beverage companies and environmental testing laboratories. The Company also sells to various universities and government agencies worldwide. The Company s technical support staff works closely with its customers in developing and implementing applications that meet their full range of analytical requirements.

The Company does not rely on any single customer or one group of customers for a material portion of its sales. During fiscal years 2006 and 2005, no single customer accounted for more than 3% of the Company s net sales.

Sales and Service

The Company has one of the largest sales and service organizations in the industry focused exclusively on its LC, MS and thermal analysis installed base. Across these product technologies, using respective specialized sales and service forces, the Company serves its customer base with approximately 2,400 field representatives in 82 sales offices throughout the world as of December 31, 2006, compared to approximately 2,400 field representatives in 87 sales offices as of December 31, 2005. The Company s sales representatives have direct responsibility for account relationships, while service representatives work in the field to install instruments and minimize instrument downtime for customers. Technical support representatives work directly with customers, helping them to develop applications and procedures. The Company provides customers with comprehensive product literature and also makes consumable products available through a dedicated catalog.

Manufacturing

The Company provides high quality LC products by controlling each stage of production of its instruments, columns and chemical reagents. The Company currently assembles a substantial portion of its LC instruments at its facility in Milford, Massachusetts, where it performs machining, assembly and testing. The Milford facility maintains a Quality Management System in accordance with the requirements of ISO 9001:2000, ISO 13485:2003 and applicable regulatory requirements (including FDA QSR and the European IVD Directives). The Company outsources manufacturing of certain electronic components such as computers, monitors and circuit boards to outside vendors that can meet the Company s quality requirements. In 2006, the Company transitioned the manufacturing of the Alliance HPLC instrument system to a company in Singapore. The Company expects to continue to pursue other outsourcing opportunities in the future. During 2006, the Company added four manufacturing locations in connection with the ERA, VICAM and Thermometrics acquisitions. ERA manufactures environmental proficiency kits in Arvada, Colorado. VICAM manufactures antibody resin and magnetic beads that are packed into columns and kits in Watertown, Massachusetts and Nixa, Missouri. Thermometrics manufactures high performance microcalorimeters in Sweden.

The Company manufactures its LC columns at its facilities in Taunton, Massachusetts and Wexford, Ireland, where it processes, sizes and treats silica and polymeric media that are packed into columns, solid phase extraction cartridges and bulk shipping containers. The Wexford facility also manufactures and distributes certain data, instruments and software components for the Company s LC, MS and thermal analysis product lines. These facilities meet the same ISO and FDA standards met by the Milford, Massachusetts facility and are registered with the FDA.

The Company manufactures most of its MS products at its facilities in Manchester, England, Cheshire, England and Wexford, Ireland. Certain components or modules of the Company s MS instruments are

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manufactured by long-standing outside contractors. Each stage of this supply chain is closely monitored by the Company to maintain its high quality and performance standards. The instruments, components or modules are then returned to the Company s facilities where its engineers perform final assembly, calibrations to customer specifications and quality control procedures. The Company s MS facilities meet similar ISO and FDA standards met by the Milford, Massachusetts facility and are registered with the FDA.

Thermal analysis and rheology products are manufactured at TA. Thermal analysis products are manufactured at the Company s New Castle, Delaware facility. Rheometry products are manufactured at the Company s New Castle, Delaware and Crawley, England facilities. Similar to MS, certain elements of TA s products are manufactured by outside contractors and are then returned to the Company s facilities for final assembly, calibration and quality control. The Company s thermal analysis facilities are certified to ISO 9001:2000 standards.

Research and Development

The Company maintains an active research and development program focused on the development and commercialization of products that both complement and update the existing product offering. The Company s research and development expenditures for 2006, 2005 and 2004 were $77.3 million, $66.9 million and $65.2 million, respectively. Included in the 2006 expense is $5.1 million associated with the adoption of Statement of Financial Accounting Standard (SFAS) No. 123(R), Share-based Payment . Nearly all of the current LC products of the Company have been developed at the Company s main research and development center located in Milford, Massachusetts, with input and feedback from the Company s extensive field organizations. The majority of the MS products have been developed at facilities in England and nearly all of the current thermal analysis products have been developed at the Company s research and development center in New Castle, Delaware. At December 31, 2006, there were approximately 571 employees involved in the Company s research and development efforts, compared to 555 employees in 2005. The Company has increased research and development expenses relating to acquisitions and the Company s continued commitment to invest significantly in new product development and existing product enhancements. Despite the Company s active research and development programs, there can be no assurances that the Company s product development and commercialization efforts will be successful or that the products developed by the Company will be accepted by the marketplace.

Employees

The Company employed approximately 4,700 employees, with 45% located in the United States, and approximately 4,500 employees, with 47% located in the United States, at December 31, 2006 and 2005, respectively. The increase of 4% over 2005 is primarily due to increases in manufacturing operations, research and development and from acquisitions. The Company considers its employee relations, in general, to be good. The Company s employees are not unionized or affiliated with any internal or external labor organizations. The Company believes that its future success depends, in a large part, upon its continued ability to attract and retain highly skilled employees. In February 2006, the Company implemented a cost reduction and expense reallocation plan, primarily in the U.S. and Europe, resulting in the employment of approximately 74 employees being terminated, all of which had left the Company as of December 31, 2006.

Competition

The analytical instrument and systems market is competitive. The Company encounters competition from several worldwide instrument manufacturers in both domestic and foreign markets for each of its three technologies. The Company competes in its markets primarily on the basis of instrument performance, reliability and service and, to a lesser extent, price. Some competitors businesses are generally more diversified and less focused on the Company s primary instrument markets. Some competitors have greater financial and other resources than the Company.

In the markets served by LC, MS and LC-MS, the Company s principal competitors include: Applied BioSystems, Inc., Agilent Technologies, Inc., Thermo Fisher Scientific Inc., Varian, Inc., Shimadzu Corporation and Bruker BioSciences Corporation. In the markets served by TA, the Company s principal competitors include: PerkinElmer Inc., Mettler-Toledo International Inc., NETZSCH-Geraetebau GmbH, Thermo Fisher Scientific Inc.,

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Malvern Instruments Ltd. and Anton-Paar. The Company is not currently aware of a competitor that it believes offers an instrument system comparable to its ACQUITY UPLC.

The market for consumable HPLC products, including separation columns, is highly competitive and more fragmented than the analytical instruments market. The Company encounters competition in the consumable columns market from chemical companies that produce column chemicals and small, specialized companies that pack and distribute columns. The Company believes that it is one of the few suppliers that process silica, packs columns, and distributes its own product. The Company competes in this market on the basis of reproducibility, reputation and performance and, to a lesser extent, price. The Company s principal competitors for consumable products include: Phenomenex, Supelco Inc., Agilent Technologies, Inc., Alltech International Holdings, Inc., Thermo Fisher Scientific Inc. and Merck and Co., Inc. The ACQUITY UPLC instrument is designed to offer a predictable level of performance when used with ACQUITY UPLC columns to effect the chemical separation. UPLC columns are both fluidically and electronically connected to the ACQUITY UPLC instrument to allow users to simultaneously employ and track the performance status of the UPLC column. The Company believes that the expansion of ACQUITY UPLC technology will enhance its chromatographic column business because of the high level of synergy between ACQUITY UPLC columns and the ACQUITY UPLC instrument.

Patents, Trademarks and Licenses

The Company owns a number of United States and foreign patents and has patent applications pending in the United States and abroad. Certain technology and software is licensed from third parties. The Company also owns a number of trademarks. The Company s patents, trademarks and licenses are viewed as valuable assets to its operations. However, the Company believes that no one patent or group of patents, trademark or license is, in and of itself, essential to the Company such that its loss would materially affect the Company s business as a whole.

Environmental Matters

The Company is subject to federal, state and local laws, regulations and ordinances that (i) govern activities or operations that may have adverse environmental effects, such as discharges to air and water, as well as handling and disposal practices for solid and hazardous wastes, and (ii) impose liability for the costs of cleaning up and certain damages resulting from sites of past spills, disposals or other releases of hazardous substances. The Company believes that it currently conducts its operations, and in the past has operated its business, in substantial compliance with applicable environmental laws. From time to time, operations of the Company have resulted or may result in noncompliance with, or liability for cleanup pursuant to environmental laws. The Company does not currently anticipate any material adverse effect on its operations, financial condition or competitive position as a result of its efforts to comply with environmental laws.

Available Information

The Company files all required reports with the Securities and Exchange Commission (SEC). The public may read and copy any materials the Company files with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

The Company is an electronic filer and the SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of the SEC electronic filing web-site is http://www.sec.gov. The Company also makes available free of charge on its web-site its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. The

Internet address for Waters Corporation is http://www.waters.com and SEC filings can be found under the caption About Waters > Investor Information.

Forward-Looking Statements

Certain of the statements in this Form 10-K and the documents incorporated in this form may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E

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of the Securities Exchange Act of 1934, as amended (the Exchange Act), regarding future results and events, including statements regarding, among other items, (i) the impact of the Company s new products, (ii) the Company s growth strategies, including its intention to make acquisitions and introduce new products, (iii) anticipated trends in the Company s business and (iv) the Company s ability to continue to control costs and maintain quality. You can identify these forward-looking statements by the use of the words believes , anticipates , plans , expects , may , will , wo intends , estimates , projects , and similar expressions, whether in the negative or affirmative. These statements are subject to various risks and uncertainties, many of which are outside the control of the Company, including and without limitation, fluctuations in capital expenditures by our customers, in particular large pharmaceutical companies, regulatory and/or administrative obstacles to the timely completion of purchase order documentation, introduction of competing products by other companies, such as improved research-grade mass spectrometers, higher speed and/or more sensitive liquid chromatographs, pressures on prices from competitors and/or customers, regulatory obstacles to new product introductions, lack of acceptance of new products, other changes in the demands of the Company s healthcare and pharmaceutical company customers, risks associated with lawsuits and other legal actions particularly involving claims for infringement of patents and other intellectual property rights, and foreign exchange rate fluctuations potentially adversely affecting translation of the Company s future non-U.S. operating results as well as additional risk factors set forth below. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements, whether because of these factors or for other reasons. The Company does not assume any obligation to update any forward-looking statements.

Item 1A: ***Risk Factors***

Competition and the Analytical Instrument Market:
The analytical instrument market and, in particular, the portion related to the Company s HPLC, UPLC, MS, LC-MS, thermal analysis and rheometry product lines, is highly competitive, and the Company encounters competition from several international instrument manufacturers and other companies in both domestic and foreign markets. Some competitors businesses are generally more diversified and less focused on the Company s primary instrument markets. There can be no assurances that the Company s competitors will not introduce more effective and less costly products than those of the Company, or that the Company will be able to increase its sales and profitability from new product introductions. There can be no assurances that the Company s sales and marketing forces will compete successfully against its competitors in the future.

Additionally, the analytical instrument market may, from time to time, experience low sales growth. Approximately 52% and 54% of the Company s net sales in 2006 and 2005, respectively, were to the worldwide pharmaceutical and biotechnology industries, which may be periodically subject to unfavorable market conditions and consolidations. Unfavorable industry conditions could have a material adverse effect on the Company s results of operations or financial condition.

Risk of Disruption:
The Company manufactures LC instruments at facilities in Milford, Massachusetts and Singapore, separation columns at its facilities in Taunton, Massachusetts and Wexford, Ireland, MS products at its facilities in Manchester, England, Cheshire, England and Wexford, Ireland, thermal analysis products at its facility in New Castle, Delaware and rheometry products at its facilities in New Castle, Delaware and Crawley, England. Any prolonged disruption to the operations at any of these facilities, whether due to labor difficulties, destruction of or damage to either facility or other reasons, could have a material adverse effect on the Company s results of operations or financial condition.

Foreign Operations and Exchange Rates:
Approximately 68% and 66% of the Company s 2006 and 2005 net sales, respectively, were outside of the United States and were primarily denominated in foreign currencies. As a result, a significant portion of the Company s sales and operations are subject to certain risks, including adverse developments in the foreign political and economic

environment, tariffs and other trade barriers, difficulties in staffing and managing foreign operations and potentially adverse tax consequences.

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Additionally, the U.S. dollar value of the Company s net sales varies with currency exchange rate fluctuations. Significant increases in the value of the U.S. dollar relative to certain foreign currencies could have a material adverse effect on the Company s results of operations or financial condition.

Reliance on Key Management:
The operation of the Company requires managerial and operational expertise. None of the key management employees has an employment contract with the Company, and there can be no assurance that such individuals will remain with the Company. If, for any reason, such key personnel do not continue to be active in management, the Company s results of operations or financial condition could be adversely affected.

Protection of Intellectual Property:
The Company vigorously protects its intellectual property rights and seeks patent coverage on all developments that it regards as material and patentable. However, there can be no assurances that any patents held by the Company will not be challenged, invalidated or circumvented or that the rights granted thereunder will provide competitive advantages to the Company. Conversely, there could be successful claims against the Company by third party patent holders with respect to certain Company products that may infringe the intellectual property rights of such third parties. The Company s patents, including those licensed from others, expire on various dates. If the Company is unable to protect its intellectual property rights, it could have an adverse and material effect on the Company s results of operations or financial condition.

Reliance on Customer Demand:
The demand for the Company s products is dependent upon the size of the markets for its LC, MS, thermal analysis and rheometry products, the level of capital expenditures of the Company s customers, the rate of economic growth in the Company s major markets and competitive considerations. There can be no assurances that the Company s results of operations or financial condition will not be adversely impacted by a change in any of the factors listed above.

Reliance on Suppliers:
Most of the raw materials, components and supplies purchased by the Company are available from a number of different suppliers; however, a number of items are purchased from limited or single sources of supply and disruption of these sources could have a temporary adverse effect on shipments and the financial results of the Company. The Company believes alternative sources could ordinarily be obtained to supply these materials, but a prolonged inability to obtain certain materials or components could have an adverse effect on the Company s financial condition or results of operations and could result in damage to its relationships with its customers and, accordingly, adversely affect the Company s business.

Reliance on Outside Manufacturers:
Certain components or modules of the Company s MS instruments are manufactured by long-standing outside contractors. In 2006, the Company transitioned the manufacturing of the Alliance HPLC instrument system to a company in Singapore. Disruptions of service by these outside contractors could have an adverse effect on the supply chain and the financial results of the Company. The Company believes that it could obtain alternative sources for these components or modules, but a prolonged inability to obtain these components or modules could have an adverse effect on the Company s financial condition or results of operations.

Item 1B: ***Unresolved Staff Comments***

None.

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Item 2: ***Properties***

Waters operates 21 United States facilities and 71 international facilities, including field offices. The Company believes its facilities are suitable and adequate for its current production level and for reasonable growth over the next several years. The Company s primary facilities are summarized in the table below.

Primary Facility Locations

Location	Function (1)	Owned/Leased
Franklin, MA	D	Leased
Milford, MA	M, R, S, A	Owned
Taunton, MA	M	Owned
Watertown, MA	M, R, S, A	Leased
Nixa, MO	M, S, D, A	Leased
Arvada, CO	M, R, S, D, A	Leased
Etten-Leur, Netherlands	S, D, A	Owned
St. Quentin, France	S, A	Leased
Singapore	S, D, A	Leased
Tokyo, Japan	S, A	Leased
Wexford, Ireland	M, D, A	Owned
New Castle, DE	M, R, S, D, A	Leased
Crawley, England	M, R, S, D, A	Leased
Cheshire, England	M, R, D, A	Leased
Manchester, England	M, R, S, A	Leased
Romania	R, A	Leased
Sweden	M, R, D, S, A	Leased

(1) M = Manufacturing; R = Research; S = Sales and service; D = Distribution; A = Administration

The Company operates and maintains 12 field offices in the United States and 59 field offices abroad in addition to sales offices in the primary facilities listed above. The Company s field office locations are listed below.

Field Office Locations (2)

United States	International		
Dublin, CA	Australia	India	Switzerland
Irvine, CA	Austria	Ireland	Taiwan
Schaumburg, IL	Belgium	Italy	United Kingdom
Wood Dale, IL	Brazil	Japan	
Beverly, MA	Canada	Korea	
Columbia, MD	Czech Republic	Mexico	
Ann Arbor, MI	Denmark	Netherlands	

Cary, NC	Finland	People s Republic of China
Parsippany, NJ	France	Poland
Huntingdon, PA	Germany	Puerto Rico
Bellaire, TX	Hong Kong	Spain
Spring, TX	Hungary	Sweden

(2) The Company operates more than one office within certain states and foreign countries.

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Item 3: ***Legal Proceedings***

Hewlett-Packard Company:
The Company filed suit in the United States against Hewlett-Packard Company and Hewlett-Packard GmbH (collectively, HP), seeking a declaration that certain products sold under the mark Alliance did not constitute an infringement of one or more patents owned by HP or its foreign subsidiaries (the HP patents). The action in the United States was dismissed for lack of controversy. Actions seeking revocation or nullification of foreign HP patents were filed by the Company in Germany, France and England. A German patent tribunal found the HP German patent to be valid. In Germany, France and England, HP and its successor, Agilent Technologies Deutschland GmbH (Agilent), brought actions alleging that certain features of the Alliance pump may infringe the HP patents. In England, the Court of Appeal found the HP patent valid and infringed. The Company s petitions for leave to appeal to the House of Lords were denied. A trial on damages was scheduled for November 2004.

In March 2004, Agilent brought a new action against the Company alleging that certain features of the Alliance pump continued to infringe the HP patents. At a hearing held in the UK in June 2004, the UK court postponed the previously scheduled November 2004 damages trial until March 2005. Instead, the court scheduled the trial in the new action for November 2004. In December 2004, following a trial in the new action, the UK court ruled that the Company did not infringe the HP patents. Agilent filed an appeal in that action, which was heard in July 2005, and the UK Appellate Court upheld the lower court s ruling of non-infringement. The damages trial scheduled for March 2005 was postponed pending this appeal and rescheduled for December 2005. In December 2005, a trial on damages commenced in the first action and continued for six days prior to a holiday recess. In February 2006, the Company, HP and Agilent entered into a settlement agreement (the Agilent Settlement Agreement) with respect to the first action and a consent order dismissing the case was entered. The Agilent Settlement Agreement provides for the release of the Company and its UK affiliate from each and every claim under Agilent s European patent (UK) number 309,596 arising out of the prior sale by either of them of Alliance Separations Modules incorporating the patented technology. In consideration of entering into the Agilent Settlement Agreement and the consent order, the Company made a payment to Agilent of 3.5 million British Pounds, in full and final settlement of Agilent s claim for damages and in relation to all claims for costs and interest in the case.

In France, the Paris District Court has found the HP patent valid and infringed by the Alliance pump. The Company appealed the French decision and, in April 2004, the French appeals court affirmed the Paris District Court s finding of infringement. The Company has filed a further appeal in the case. The Company has sought a declaration from the French court that, as was found in both the UK and Germany, certain modified features of the Alliance pump do not infringe the HP patents. A hearing on this matter is currently scheduled for June 2007. In the German case, a German court has found the patent infringed. The Company appealed the German decision and, in December 2004, the German appeals court reversed the trial court and issued a finding of non-infringement in favor of the Company. Agilent is seeking an appeal in that action and, in July 2005, brought a new action against the Company alleging that certain features of the Alliance pump continue to infringe the HP patents. In August 2006, following a trial in this new action the German court ruled that the Company did not infringe the HP patents. Agilent has filed an appeal in this action.

The Company recorded provisions in the quarters ended June 30, 2002, April 3, 2004, and December 31, 2005 for estimated damages, legal fees, and court costs incurred with respect to this ongoing litigation. The provisions represent management s best estimate of the probable and reasonably estimable loss related to the litigations.

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

None.

EXECUTIVE OFFICERS OF THE REGISTRANT

Officers of the Company are elected annually by the Board of Directors and hold office at the discretion of the Board of Directors. The following persons serve as executive officers of the Company:

Douglas A. Berthiaume, 58, has served as Chairman of the Board of Directors of the Company since February 1996 and has served as Chief Executive Officer and a Director of the Company since August 1994. Mr. Berthiaume

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also served as President of the Company from August 1994 to January 2002. In March 2003, Mr. Berthiaume once again became President of the Company. From 1990 to 1994, Mr. Berthiaume served as President of the Waters Chromatography Division of Millipore. Mr. Berthiaume is the Chairman of the Children s Hospital Trust Board, and a Trustee of the Children s Hospital Medical Center, The University of Massachusetts Amherst Foundation and a Director of Genzyme Corporation.

Arthur G. Caputo, 55, became an Executive Vice President in March 2003 and has served as President of the Waters Division since January 2002. Previously, he was the Senior Vice President, Worldwide Sales and Marketing of the Company since August 1994. He joined Millipore in October 1977 and held a number of positions in sales. Previous roles include Senior Vice President and General Manager of Millipore s North American Business Operations responsible for establishing the Millipore North American Sales Subsidiary and General Manager of Waters North American field sales, support and marketing functions.

Elizabeth B. Rae, 49, became Vice President of Human Resources in October 2005 and has served as Vice President of Worldwide Compensation and Benefits since January 2002. She joined Waters Corporation in January 1996 as Director of Worldwide Compensation. Prior to joining Waters she has held senior human resources positions in retail, healthcare and financial services companies.

John Ornell, 49, became Vice President, Finance and Administration and Chief Financial Officer in June 2001. He joined Millipore in 1990 and previously served as Vice President, Operations. During his years at Waters, he has also been Vice President of Manufacturing and Engineering, had responsibility for Operations Finance and Distribution and had a senior role in the successful implementation of the Company s worldwide business systems.

Mark T. Beaudouin, 52, became Vice President, General Counsel and Secretary of the Company in April 2003. Prior to joining Waters, he served as Senior Vice President, General Counsel and Secretary of PAREXEL International Corporation, a bio/pharmaceutical services company, from January 2000 to April 2003. Previously, from May 1985 to January 2000, Mr. Beaudouin served in several senior legal management positions, including Vice President, General Counsel and Secretary of BC International, Inc., a development stage biotechnology company, First Senior Vice President, General Counsel and Secretary of J. Baker, Inc., a diversified retail company, and General Counsel and Secretary of GenRad, Inc., a high technology test equipment manufacturer.

PART II

Item 5: ***Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

Equity compensation plan information is incorporated by reference from Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters, of this document, and should be considered an integral part of this Item 5. The Company s Common Stock is registered under the Securities Exchange Act of 1934, as amended (the Exchange Act), and is listed on the New York Stock Exchange under the symbol WAT. As of February 23, 2007, the Company had approximately 247 common stockholders of record. The Company has not declared or paid any dividends on its Common Stock in its past three fiscal years and does not plan to pay dividends in the foreseeable future.

The Company has not made any sales of unregistered securities in the years ended December 31, 2006, 2005 or 2004.

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STOCK PRICE PERFORMANCE GRAPH

The following graph compares the cumulative total return on $100 invested as of December 31, 2001 (the last day of public trading of the Company s Common Stock in fiscal year 2001) through December 29, 2006 (the last day of public trading of the Common Stock in fiscal year 2006) in the Company s Common Stock, the NYSE Market Index and the SIC Code 3826 Index. The return of the indices is calculated assuming reinvestment of dividends during the period presented. The Company has not paid any dividends since its initial public offering. The stock price performance shown on the graph below is not necessarily indicative of future price performance.

COMPARISON OF CUMULATIVE TOTAL RETURN SINCE DECEMBER 31, 2001 AMONG WATERS CORPORATION, NYSE MARKET INDEX AND SIC CODE 3826 LABORATORY ANALYTICAL INSTRUMENTS

	2001	2002	2003	2005	2005	2006
WATER CORPORATION	100.00	56.21	85.57	120.75	97.55	126.37
SIC CODE INDEX	100.00	51.13	74.59	91.53	94.40	107.64
NYSE MARKET INDEX	100.00	81.69	105.82	119.50	129.37	151.57

The quarterly range of high and low sales prices for the Common Stock as reported by the New York Stock Exchange is as follows:

	Price Range	
For the quarter ended	**High**	**Low**
April 2, 2005	$ 51.57	$ 35.51
July 2, 2005	$ 40.85	$ 33.99
October 1, 2005	$ 46.43	$ 37.42
December 31, 2005	$ 43.79	$ 35.11
April 1, 2006	$ 44.88	$ 37.06
July 1, 2006	$ 46.98	$ 40.40
September 30, 2006	$ 45.41	$ 38.38
December 31, 2006	$ 51.64	$ 44.43

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The following table provides information about purchases by the Company during the three months ended December 31, 2006 of equity securities registered by the Company under to the Exchange Act (in thousands, except per share data):

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs (2)	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Programs
October 1 to 28, 2006		$		$ 56,144
October 29 to November 25, 2006				56,144
November 26 to December 31, 2006	430	49.85	430	34,709
Total	430	49.85	430	34,709

(1) The Company purchased an aggregate of 11.3 million shares of its common stock in open market transactions pursuant to a repurchase program (the Program) that was announced on October 25, 2005.

(2) The Company s Board of Directors approved the repurchase by the Company of up to $500.0 million of its outstanding common stock pursuant to the Program. The expiration date of the Program is October 25, 2007.

Item 6: ***Selected Financial Data***

Reference is made to information contained in the section entitled Selected Financial Data on page 77 of this Form 10-K, included in Item 8, Financial Statements and Supplementary Data.

Item 7: ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Business and Financial Overview:

The Company s sales were $1,280.2 million, $1,158.2 million and $1,104.5 million in 2006, 2005 and 2004, respectively. Sales grew 11% in 2006 over 2005 and 5% in 2005 over 2004. Overall, the sales growth achieved in these years can be primarily attributed to the Company s introduction of new products and sustained growth in Asia. The 2006 and 2005 sales growth benefited from the introduction of the ACQUITY UPLC® and the Quattro Premier™ XE based systems and an increase in chemistry consumable sales. In addition, the 2006 sales growth also benefited from the introduction of the new SQD, TQD and Synapt™ HDMS mass spectrometry systems which were introduced in the second-half of 2006.

The effect of currency translation benefited the 2006 sales growth rate by less than 1%, principally in Europe, and was neutral to the 2005 sales growth rates. U.S. sales increased 4% and 2%; European sales grew 12% and 3%; and Asian

sales (including Japan) grew 19% and 10% during 2006 and 2005, respectively. Asian sales growth was strongest in India and China.

In 2006, global sales to pharmaceutical customers rebounded from 2005 levels and industry-wide sales grew 8%, as these customers increased their capital spending on the Company s new products. Global sales to pharmaceutical customers were weak in 2005 as the Company s large pharmaceutical customers decreased capital spending as these customers dealt with various new drug pipeline, merger and acquisition and litigation issues. Global sales to industrial and food safety customers continued its positive trend as sales grew 13% in 2006 over 2005. The TA Division (TA) sales, a business with a heavy industrial focus, grew 9% and 8% for 2006 and 2005, respectively, and the sales growth can be attributed to new product introductions and expansion of its Asian businesses.

The Waters Division sales grew by 11% in 2006 and 4% in 2005. The Waters Division s products and services consist of LC & MS instrument systems which include high performance liquid chromatography (HPLC), ultra performance liquid chromatography (UPLC and together with HPLC, herein referred to as LC), mass

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spectrometry (MS) products, chemistry consumable products, and LC and MS services. The sales growth is strongly influenced by ACQUITY UPLC sales and sales growth in the chemistry consumables business.

In 2006, the Company continued to enhance its operations in Asia by expanding an existing partnership to manufacture instrumentation in Singapore. The Company transitioned the manufacturing of the Alliance® instrument system and, while the Company expects to achieve cost savings efficiencies in the future, the overall impact during the ramp-up in 2006 was slightly negative on gross profit margin percentages in 2006 compared to 2005.

Operating income was $295.2 million, $283.2 million and $284.9 million in 2006, 2005 and 2004, respectively. Operating income was primarily impacted by the following:

The $12.0 million net increase in 2006 operating income from 2005 is primarily a result of the increased sales volume being partially offset by the $28.0 million of the additional stock-based compensation costs incurred as a result of the adoption of Statement of Financial Accounting Standard (SFAS) No. 123(R) Share-Based Payment and $8.5 million of restructuring costs incurred relating to the February 2006 cost reduction initiative. The Company does not expect to incur any significant additional restructuring costs for this initiative in the future.

The $1.7 million net decrease in operating income in 2005 from 2004 is primarily attributable to a litigation provision of $3.1 million related to a patent litigation settlement with Hewlett-Packard Company in February 2006 that was recorded in the fourth quarter of 2005. The remaining increase in 2005 operating income was primarily a result of sales growth. The 2004 operating income included the benefit of a litigation judgment in the amount of $17.1 million from Perkin-Elmer Corporation partially offset by litigation provisions of $7.8 million and a technology license asset impairment of $4.0 million.

The Company continuously evaluates its equity investments for impairment and, as a result, the Company recorded, in net other expense, a net write-down of certain equity investments in the amount of $5.8 million, $3.1 million and $1.0 million in 2006, 2005 and 2004, respectively. Included in the 2005 net write-down is a gain on the sale of an equity investment of $1.7 million.

Operating cash flow was $263.6 million, $298.1 million and $259.4 million in 2006, 2005 and 2004, respectively. Included in the 2006 operating cash flow was a $9.0 million tax payment associated with the American Jobs Creation Act (AJCA), a $3.5 million litigation payment and $7.0 million of severance and other facility related payments made in connection with the cost reduction initiative. The 2005 operating cash flow included an AJCA payment of approximately $10.0 million. The decline in the 2006 operating cash flow can also be attributed to an increase in inventories of $29.9 million over 2005. The inventory increase is attributable to the ramp-up of new product introductions and an increase in the safety stock levels resulting from the outsourcing of the Alliance instrument system manufacturing. Operating cash flows continue to benefit from the improvement in accounts receivable collection measured in days-sales-outstanding (DSO). DSO s were 64 days, 70 days and 76 days at December 31, 2006, 2005 and 2004, respectively.

In cash flows used in investing activities, capital expenditures related to property, plant, equipment, software capitalization and other intangibles were $51.4 million, $51.0 million and $66.2 million, in 2006, 2005 and 2004, respectively. Capital expenditures have remained substantially unchanged over the last three years. Capital expenditures in 2004 included $18.1 million for the purchase of a building adjacent to the Company s headquarters.

The Company continues to evaluate the acquisition of businesses, product lines and technologies to augment the Waters and TA operating divisions. On December 15, 2006, the Company acquired all of the outstanding capital stock of Environmental Resources Associates, Inc., (ERA), a provider of environmental testing products for quality control,

proficiency testing and specialty calibration chemicals used by environmental laboratories, for approximately $62.5 million in cash and the assumption of $3.8 million of debt. The Company expects that ERA will add approximately $17.0 million of product sales and be about neutral to earnings in 2007 after debt service costs. In February 2006, the Company acquired the net assets of the food safety business of VICAM Limited Partnership (VICAM) for approximately $13.8 million. VICAM products added approximately $8.0 million to sales and were about neutral to earnings for the year ended December 31, 2006 after debt service costs. VICAM product sales in 2007 are expected to be approximately $10.0 million. In August 2006, the Company acquired all of

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the outstanding capital stock of Thermometric AB (Thermometrics), a manufacturer of high performance microcalorimeters, for a total of $2.5 million in cash and the assumption of $1.2 million of debt. Thermometrics products added approximately $1.5 million to sales and were neutral to earnings for the year ended December 31, 2006. Thermometrics sales are expected to be approximately $4.0 million in 2007.

During 2006, management continued to apply the Company s net cash flow to repurchase shares of Company stock through the $500.0 million program authorized by the Company s Board of Directors in October 2005. During 2006, the Company purchased 5.8 million shares of its common stock at a cost of $249.2 million. The Company has repurchased an aggregate of 11.3 million shares of its common stock under this program at a cost of $465.3 million, leaving $34.7 million authorized for future repurchases. The Company believes that the share repurchase programs are beneficial to shareholders by increasing earnings per share through reducing the number of outstanding shares. The Company also believes that it has the financial flexibility to fund these share repurchases given current cash and debt levels, and invest in research, technology and business acquisitions to further grow the Company s sales and profits.

In January 2007, the Company terminated multiple term loan and revolving credit agreements entered into 2005 and 2004. The Company refinanced the credit agreement facilities to expand its debt capacity to $1.1 billion, reduce its borrowing rates and extend the maturity by two years.

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005

Net Sales:
Net sales for 2006 and 2005 were $1,280.2 million and $1,158.2 million, respectively, an increase of 11%. Foreign currency translation benefited the 2006 sales growth rate by less than 1%. Product sales were $922.5 million and $834.7 million for 2006 and 2005, respectively, an increase of 11% over 2005. The increase in product sales was primarily due to the overall positive growth in LC, MS and TA instrument systems sales, an increase in chemistry consumables sales and the effect of acquisitions. Service sales were $357.7 million and $323.6 million in the 2006 and 2005, respectively, an increase of 11%. The increase was primarily attributable to growth in the Company s installed base of instruments and higher sales of service contracts.

The following commentary discusses the Company s sales performance by product line.

Waters Division Net Sales:
The Waters Division sales grew approximately 11% in 2006. The effect of foreign currency translation benefited the 2006 Waters Division sales growth by less than 1%. Chemistry consumables sales grew approximately 18% in 2006. This growth was driven by increased column sales of ACQUITY UPLC proprietary column technology, new XBridge™ columns, Oasis® sample preparation products and the sales associated with the acquired VICAM product line. LC and MS service sales grew 9% in 2006 due to increased sales of service plans to the higher installed base of customers. LC and MS instrument systems sales grew 9% in 2006. The increase in LC and MS instrument sales during 2006 is primarily attributable to higher sales of ACQUITY UPLC systems and higher MS triple quadrupole system sales, offset by a decline in lower-end MS systems sales. Waters Division sales by product mix was substantially unchanged in 2006 and 2005 with instruments, chemistry and service representing approximately 57%, 16% and 27% respectively. Geographically, Waters Division sales in the U.S., Europe and Asia (including Japan) strengthened approximately 4%, 12% and 19%, respectively, in 2006. The effects of foreign currency translation increased sales growth by 2% in Europe and decreased sales growth in Asia by 3% in 2006. The growth in Europe was broad-based across most major countries, particularly in Eastern Europe, while Asia s growth was primarily driven by increased sales in India and China. U.S. sales growth in 2006 was primarily due to higher demand from the Company s pharmaceutical and industrial customers.

TA Division Net Sales:

TA Division s sales grew 9% in 2006 as a result of TA s new product introductions and expansion of its Asian businesses. Foreign currency translation had no impact to this overall sales growth rate. Instrument sales grew 4% as TA introduced four new differential scanning calorimeters during 2006 and, in late August 2006, the Company entered the field of microcalorimetry through the acquisition of Thermometrics. Instrument system sales represented approximately 70% and 73% of sales in 2006 and 2005, respectively. TA service sales grew 22% in 2006 and

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can be attributed to the increased sales of service plans to the higher installed base of customers. Geographically, sales growth for 2006 was predominantly in Europe and Asia.

Gross Profit:
Gross profit for 2006 was $744.0 million compared to $679.9 million for 2005, an increase of $64.1 million or 9% and is generally consistent with the increase in net sales. Gross profit as a percentage of sales decreased to 58.1% in 2006 from 58.7% in 2005. The 2006 gross profit was negatively impacted by $4.3 million of stock-based compensation costs relating to the adoption of SFAS No. 123(R). The remaining slight decrease in gross profit percentage in 2006 as compared to 2005 is primarily due to product transition costs to Singapore and product introduction costs on new MS instruments.

Selling and Administrative Expenses:
Selling and administrative expenses for 2006 and 2005 were $357.7 million and $321.7 million, respectively. As a percentage of net sales, selling and administrative expenses were 27.9% for 2006 compared to 27.8% for 2005. The $36.0 million or 11% increase in total selling and administrative expenses for 2006 is primarily due to additional stock-based compensation costs of $18.6 million, annual merit increases across most divisions, other headcount additions and related fringe benefits and indirect costs of $11.6 million. Other increases in selling and administration expenses were offset by decreases related to the February 2006 cost saving initiative. The Company has made investments in Asia, largely in the second half of 2006, in support of growing business opportunities and management expects expenses to continue to grow at a modest rate in the future as compared to 2006.

Research and Development Expenses:
Research and development expenses were $77.3 million for 2006 and $66.9 million for 2005, an increase of $10.4 million or 16% primarily due to stock-based compensation costs of $5.1 million relating to the adoption of SFAS No. 123(R)and the merit increases across most divisions, other headcount additions and related fringe benefits and indirect costs. The remaining increases in research and development expenses in 2006 as compared to 2005 reflects the costs of introducing multiple new MS instruments in the second half of 2006.

2006 Restructuring:
In February 2006, the Company implemented a cost reduction plan primarily affecting operations in the U.S. and Europe that resulted in the employment of 74 employees being terminated, all of which had left the Company as of December 31, 2006. In addition, the Company closed a sales and demonstration office in the Netherlands in the second quarter of 2006. The Company implemented this cost reduction plan primarily to realign its operating costs with business opportunities around the world.

The following is a summary of activity of the Company s 2006 restructuring liability (in thousands):

	Balance December 31, 2005	Charges	Utilization	Balance December 31, 2006
Severance	$	$ 6,443	$ (5,010)	$ 1,433
Other		2,041	(1,993)	48
Total	$	$ 8,484	$ (7,003)	$ 1,481

The Company does not expect to incur any additional charges connection with the February 2006 restructuring initiative. The Company achieved approximately $4.4 million of cost savings in 2006 from this initiative, mostly in the second half of 2006, and expects to achieve approximately $7.4 million in cost savings annually as a result of this restructuring. Other charges include approximately $0.7 million of leasehold improvement assets, net of accumulated amortization, written-off as a result of the closure of the facility in the Netherlands.

Litigation Provisions:
Litigation provisions in 2005 were $3.1 million relating to patent litigation with Agilent Corporation and Hewlett-Packard Company (Hewlett-Packard). This patent litigation was settled in February 2006 and recorded in the 2005 statement of operations. No additional provisions were made in 2006.

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Other (Expense) Income, Net:
In the fourth quarter of 2006, the Company recorded a $5.8 million charge for an other-than-temporary impairment to an equity investment in Caprion Pharmaceuticals Inc. (Caprion). The charge was recorded in 2006 when the Company learned that Caprion s financial condition had deteriorated and a merger was in process that, in the Company s assessment, would result in the Company s investment being substantially diminished. The remaining value of the Caprion investment was approximately $1.7 million as of December 31, 2006.

In the fourth quarter of 2005, the Company sold all of its equity investment in Nuvelo, Inc. and recorded a gain of $1.7 million. In the fourth quarter of 2005, the Company also recorded a $4.8 million charge for an other-than-temporary impairment for the full value of the Company s investment in Beyond Genomics, Inc. This charge was recorded based on the Company s assessment of Beyond Genomics, Inc. s financial condition.

Interest Expense:
Interest expense was $51.7 million and $24.7 million for 2006 and 2005, respectively. The increase in 2006 interest expense is primarily attributable to increases in interest rates on the Company s outstanding debt and an increase in average borrowings in the U.S. to fund the stock repurchase programs.

Interest Income:
Interest income for 2006 and 2005 was $25.3 million and $19.3 million, respectively. The increase in interest income is primarily due to higher interest rate yields.

Provision for Income Taxes:
The Company s effective tax rates for 2006 and 2005 were 15.5% and 26.4%, respectively. Included in the 2005 effective tax rate is the effect of $24.0 million of income tax expense related to the repatriation of funds from the Company s foreign subsidiaries under the ACJA. The remaining decrease in the effective tax rates for 2006 compared to 2005 is primarily attributable to the proportionate increase in income in international jurisdictions with lower effective tax rates, primarily Ireland and Singapore. In addition, the adoption of SFAS No. 123(R) resulted in the recognition of a tax benefit at a higher effective tax rate in 2006.

Year Ended December 31, 2005 Compared to Year Ended December 31, 2004

Net Sales:
Net sales in 2005 were $1,158.2 million, an increase of 5% compared to sales of $1,104.5 million in 2004. Foreign currency translation had no significant effect overall on sales growth in 2005. In 2005, product sales increased $27.9 million or 3% and service sales increased $25.8 million or 9% over sales in 2004. The increase in product sales is primarily due to the continued strength of LC, MS and TA instrument sales growth, increases in sales of chemistry consumables and, particularly, the full-year sales in 2005 of the ACQUITY UPLC system. The increase in service sales is primarily due to growth in the Company s instrument installed base and sales of service contracts.

Waters Division Net Sales:
Waters Division s sales in 2005 grew approximately 4%. The effect of foreign currency translation decreased overall sales by 1%. The growth in LC and MS instrument system sales in 2005 was 2%. This growth was due principally to the full-year impact of products introduced in 2004, such as the ACQUITY UPLC instrument, in combination with demand for existing LC instruments, and an increase in Q-Tof Premier and Quattro Premier XE system sales substantially offset by weak single quadrupole and magnetic sector instrument sales. In 2005, the sales of chemistry consumables (sample preparation devices and chromatography columns) grew 8% primarily as a result of continued strength in demand from the introduction of the new XBridge, SunFire^{tm} and ACQUITY UPLC chromatography columns and Oasis sample preparation cartridges. Service sales in 2005 grew 8% over 2004 due to increased sales of

service plans to the Company s growing installed base of customers. Service sales growth was geographically broad-based and was driven by increased demand, primarily from large multi-national customers, for service plans to maintain a higher percentage of their installed Waters instruments and their newly purchased Waters instruments. The 2005 Waters Division sales product mix for instruments, chemistry and service was approximately 57%, 16% and 27%, respectively. The 2004 Waters Division sales product mix for instruments, chemistry and service was approximately 59%, 14% and 27%, respectively.

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Geographically, Waters Division sales grew 10% in Asia and 7% in Japan while the U.S. and European sales grew 1% and 3%, respectively. Foreign currency translation had no significant impact on sales growth in 2005; except in Japan where sales were negatively impacted by 3%. Sales growth rates in Asia and Japan were driven by business associated with pharmaceutical industry demand in India and more broad-based growth in China. Increased regulations for food and drinking water testing also contributed to sales growth in Japan and in Asia.

TA Division Net Sales:
Sales for thermal analysis instruments, rheometry instruments and related service sales grew 8% in 2005. Instrument system sales grew 6% as strong demand for TA products from customers outside of the U.S. contributed to the division s overall sales growth. Instrument system sales represented approximately 73% of sales in 2005 and 2004. Sales growth for TA outside of the U.S. was 13% in 2005 compared to 2004. TA s positive sales growth performance can be attributed to the strong demand for TA s products in Japan and Asia and TA s worldwide expanded sales and marketing efforts. Sales in the U.S. and Europe grew 3% while sales in Japan and Asia grew 20% and 39% in 2005, respectively. In 2005, service sales grew approximately 15% primarily as a result of providing service to a larger installed base of instruments.

Gross Profit:
Gross profit for 2005 was $679.9 million compared to $649.7 million for 2004, an increase of $30.2 million or 5% and generally consistent with the increase in net sales. Gross profit as a percentage of sales decreased to 58.7% in 2005 from 58.8% in 2004. The slight decline in gross profit percentage is primarily attributable to a higher mix of more costly new products, in particular the ACQUITY UPLC instrument, as well as lower sales of higher margin MS instruments. These factors negatively affecting gross profit percentage were partially offset by an increased mix of higher margin chemistry consumables and service sales.

Selling and Administrative Expenses:
Selling and administrative expenses for 2005 and 2004 were $321.7 million and $300.2 million, respectively. As a percentage of net sales, selling and administrative expenses increased to 27.8% for 2005 from 27.2% for 2004. The $21.5 million or 7% increase in total selling and administrative expenses for 2005 is primarily attributable to the following: an increase of approximately $4.1 million as a result of foreign currency effects; annual merit increases and other headcount additions and related fringe benefits and indirect costs of approximately $15.4 million; an increase in travel expenses of approximately $6.4 million; and an increase in expenses associated with a new building in Milford, Massachusetts acquired in 2004. The impact of these increases was primarily offset by lower sales commissions and management incentive compensation expense derived from 2005 financial results.

Research and Development Expenses:
Research and development expenses were $66.9 million for 2005 and $65.2 million for 2004, an increase of $1.7 million or 3%. The increase is primarily attributable to an increase in headcount as the Company continues to invest in the development of new and improved LC, MS, thermal analysis and rheometry products.

Litigation Provisions and Settlement:
Net litigation settlements and provisions for 2005 were a $3.1 million charge compared to a $9.3 million net benefit for 2004. In 2005, the Company recorded a provision of $3.1 million relating to patent litigation with Hewlett-Packard. This patent litigation was settled in February 2006. In 2004, the Company recorded the benefit of a litigation judgment in the amount of $17.1 million and a provision expense of $7.8 million. The benefit in 2004 is related to the conclusion of the Company s litigation with Perkin-Elmer. The provision in 2004 was related to the on-going patent infringement suit with Hewlett-Packard. In 2005, the Company made payments for legal fees regarding the Hewlett-Packard litigation in the amount of approximately $2.3 million.

Impairment of Long-Lived Asset:
In 2004, the Company recorded a $4.0 million charge for an other-than-temporary impairment of its technology license with Sandia National Laboratories, as a significant portion of the technology collaboration program was suspended. There was no such charge in 2005. The remaining value of the license was approximately $0.8 million and $1.0 million as of December 31, 2005 and 2004, respectively.

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Other (Expense) Income, Net:
In 2005, the Company sold all of its equity investment in Nuvelo, Inc. and recorded a gain of $1.7 million. In 2005, the Company also recorded a $4.8 million charge for an other-than-temporary impairment for the full value of the Company s investment in Beyond Genomics, Inc. This charge was recorded based on the Company s assessment of Beyond Genomics, Inc. s financial condition. In 2004, the Company recorded a $1.0 million pre-tax charge for an other-than-temporary impairment to the Company s remaining investment carrying value of GeneProt, Inc. This charge was recorded based on the Company s assessment of GeneProt s financial condition.

Interest Expense:
Interest expense was $24.7 million and $10.1 million for 2005 and 2004, respectively. The increase in 2005 interest expense is primarily attributable to a combination of additional borrowings in the U.S. to fund the stock repurchase programs and higher interest rates on the Company s outstanding debt.

Interest Income:
Interest income for 2005 and 2004 was $19.3 million and $11.9 million, respectively. The increase in interest income is primarily due to higher cash balances and higher interest rate yields.

Provision for Income Taxes:
In October 2004, the AJCA was signed into law. The AJCA creates a temporary incentive for U.S. multi-national corporations to repatriate accumulated income abroad by providing an 85% dividends received deduction for certain dividends from controlled foreign corporations. It previously had been the Company s practice to permanently reinvest all foreign earnings into foreign operations. On July 12, 2005, the Board of Directors of the Company approved the repatriation of $500.0 million as a qualified distribution in accordance with the AJCA. The Company has used and will continue to use the repatriated cash to fund current and future operating expenses within the parameters of Internal Revenue Service guidance. During the third quarter of 2005, the Company recorded a tax liability of $24.0 million for the federal, state and foreign taxes related to the qualified and base period distribution in accordance with SFAS No. 109, Accounting for Income Taxes .

The Company s effective tax rates for 2005 and 2004 were 26.4% and 21.6%, respectively. Included in the 2005 effective tax rate is the effect of $24.0 million of income tax expense related to the repatriation of funds from the Company s foreign subsidiaries under the AJCA. The 2004 effective tax rate was impacted by the net tax effect of the Perkin-Elmer litigation judgment received and the litigation provisions for the on-going patent infringement suit with Hewlett-Packard. The remaining change in effective tax rates is primarily attributable to the relative increase in income in international jurisdictions with lower effective tax rates, primarily Ireland.

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Liquidity and Capital Resources

Condensed Consolidated Statements of Cash Flows (in thousands):

	Year Ended December 31		
	2006	**2005**	**2004**
Net income	$ 222,200	$ 201,975	$ 224,053
Depreciation and amortization	46,159	43,685	41,926
Stock-based compensation	28,813	765	75
Deferred income taxes	506	10,235	1,468
Tax benefit related to stock option plans		4,872	32,012
Change in accounts receivable	(9,803)	(6,515)	(36,453)
Change in inventories	(29,853)	(6,973)	(11,575)
Change in accounts payable and other current liabilities	1,670	26,802	12,203
Change in accrued litigation	(4,420)	688	(16,095)
Change in deferred revenue and customer advances	1,230	7,551	1,526
Other changes	7,092	14,982	10,309
Net cash provided by operating activities	263,594	298,067	259,449
Net cash used in investing activities	(130,374)	(51,045)	(108,605)
Net cash (used in) provided by financing activities	(125,906)	(272,015)	21,507
Effect of exchange rate changes on cash and cash equivalents	13,264	(20,496)	9,945
Increase (decrease) in cash and cash equivalents	$ 20,578	$ (45,489)	$ 182,296

Cash Flow from Operating Activities

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005

Net cash provided by operating activities was $263.6 million and $298.1 million in 2006 and 2005, respectively. The $34.5 million decline in net cash provided from operating activities in 2006 compared to 2005 is attributed primarily to the following significant changes in the sources and uses of net cash provided from operating activities, aside from the increase in net income and the impact of stock compensation under SFAS 123(R):

The change in accounts receivable in 2006 compared to 2005 is primarily attributable to the timing of payments made by customers and the higher sales volume in 2006 as compared to 2005. The days-sales-outstanding (DSO) decreased to 64 days at December 31, 2006 from 70 days at December 31, 2005.

The change in inventory in 2006 compared to 2005 results from the increase in inventory due to the ramp-up of new MS products, an increase in LC instrument inventory associated with the transition to higher production levels of ACQUITY systems from Alliance systems and a planned increase in the Alliance inventory levels during the outsourcing transition.

The 2006 change in accounts payable and other current liabilities was impacted by cash payments made on increased inventory levels, severance and other facility related payments of $7.0 million in connection with the

cost reduction initiative and a litigation payment of $3.5 million to settle the Hewlett-Packard litigation.

Also included in the change in accounts payable and other current liabilities in 2006 was a tax payment in the amount of $9.0 million related to the distribution and repatriation of cash under the AJCA. During 2005, the income tax accrual was increased by $24.0 million resulting from the repatriation of funds under the AJCA.

Net cash provided from deferred revenue and customer advances in both 2006 and 2005 was a result of the installed base of customers renewing annual service contracts.

2006 net cash provided by operating activities as compared to 2005 was impacted by the adoption of SFAS No. 123(R). Under SFAS No. 123(R), $16.5 million of benefits of tax deductions in excess of recognized compensation costs were reported as cash from financing activities in 2006; prior to the adoption