

2005 Annual Report



CSI Communications Systems, Inc.

About Communications Systems, Inc.

Communications Systems, Inc. (AMEX:JCS) provides a growing family of physical and electronic connectivity infrastructure and services for voice, data and video communications. The company's product families include a broad range of copper-based and fiber optic connection devices, digital subscriber line filters and connection devices, structured wiring systems that support Local Area Networks, media conversion devices and switches.

TO OUR SHAREHOLDERS

Strong Financial Condition

Communications Systems, Inc. continues to generate cash closing the year at \$26,660,000 and the current ratio continues at a lofty 6 to 1. The Company has no long or short-term debt and equity at December 31, 2005 was of \$79,851,000

Operating Results

Two of the continuing operations of Communications Systems, Inc., Suttle and Transition Networks combined to record very satisfactory results in 2005. However, improved results over 2004 are not readily apparent without explanation. Net income includes the after tax loss in the amount of \$1,268,000 of the discontinued operations of Image Systems and Austin Taylor Communications Ltd. Discontinued operations also includes an after tax gain of \$222,000 on the sale of the inventory and equipment of Image Systems in the fourth quarter of 2005. Further, the process of converging MiLAN Technologies into Transition Networks ended the MiLAN operating losses of \$2,803,000 after 9 months which losses are included in continuing operations for 2005. The MiLAN operation for the 4th quarter resulted in operating income of \$143,000, a significant recovery.

FINANCIAL HIGHLIGHTS

(in thousands, except per share amounts)

	2005	2004	2003
Sales from Continuing Operations	\$109,709	\$100,526	\$95,771
Gross Margin from Continuing Operations	36,870	35,334	29,750
Operating Income from Continuing Operations	6,805	8,079	5,586
Net Income	4,470	4,763	2,717
Basic Net Income (loss) Per Share			
Continuing Operations	.64	.65	.52
Discontinued Operations	(.12)	(.07)	(.19)
	.52	.58	.33
Diluted Net Income (loss) Per Share			
Continuing Operations	.63	.64	.52
Discontinued Operations	(.12)	(.07)	(.19)
	.51	.57	.33
Average Dilutive Shares Outstanding	8,716	8,320	8,186
Working Capital	\$66,324	\$64,604	\$57,952
Total Assets	\$92,883	\$89,481	\$79,096
Stockholders' Equity	\$79,851	\$77,051	\$70,838

Left to Right:

Paul N. Hanson -
Chief Financial Officer, Vice President of Finance, Treasurer and Secretary

Curtis A. Sampson - Chairman and Chief Executive Officer

Jeffrey K. Berg - President and Chief Operating Officer



Transition Networks (without MiLAN) recorded \$38,572,000 in revenue and \$4,364,000 of operating income for 2005, compared to \$41,058,000 and \$4,176,000 respectively in 2004. The MiLAN operations will be consolidated and reported as Transition Networks in the future.

The Suttle operations were again the highlight in 2005 after that unit's remarkable recovery in 2004. Suttle sales increased 18% to \$47,324,000 and operating income increased \$2,149,000, or 45%, to \$6,909,000.

JDL Technologies required considerable intervention on the part of the CSI Corporate Staff and a consultant in December. The JDL revenue increased sharply for 2005 to \$15,333,000 compared to \$7,969,000 in 2004 placing a burden on the JDL management, particularly in the contract administration and project management of two of JDL's major customers. The operating loss of \$665,000 in the fourth quarter is not indicative of future operating results.

Executing Our Strategy

2005 was a very busy year for CSI and its business units. Our goal of moving forward with profitable growth business units caused CSI to sell Image Systems, one of the discontinued business units, which was sold in October. The other discontinued business unit, Austin Taylor is still in the process of a sale.

The combination of Transitions Networks and MiLAN Technology is capitalizing on the strengths and products of both operations. This integration has resulted in building a more complete product portfolio and is providing a more efficient operation. This is discussed in more detail in Dan Easter's report, which follows.

Suttle has introduced over 60 new products in a fast growing segment of their market. Significant DSL sales loss to one account will be difficult to overcome, but the Suttle Team is dedicated to replacing that business with more profitable and sustainable business. This is discussed in more detail in Dave McGraw's report, which follows.

JDL Technologies, Inc. is in process of rebounding from the difficulties and disappointments of 2005, which reduced that units operating income in 2005. Promising new revenue from several major accounts is already booked with reasonable margins. JDL will also continue to explore new lines of business and products that it can bring to the educational market. See Tom Lapping's report for greater detail on the JDL operations.

Company's Future

While we have made steady progress in many areas, as we look ahead we have more work to do.

Our experienced, talented and dedicated group of people have brought CSI and its business units through an extremely trying time in our industry. We continue to operate in an uncertain and challenging worldwide market. We are focused on these challenges of continuing profitable growth, exceeding the expectations of our customers and continuing our position as a force in providing products for the next-generation networks.



We thank you for your continued support and the trust you have placed in us.

Steven A. Simpson
Jeffrey K. Bug

SELECTED FINANCIAL INFORMATION

(in thousands, except per share amounts)

Selected Income Statement Data	2005	2004	2003	2002	2001
Sales from Continuing Operations	\$109,709	\$100,526	\$95,771	\$100,161	\$85,486
Costs and Expenses:					
Cost of Sales	72,839	65,193	66,021	72,301	60,695
Selling, General & Administrative	30,065	27,255	24,163	23,543	23,240
Total Costs and Expenses	102,904	92,448	90,184	95,844	83,935
Operating Income from Continuing Operations (1)	6,805	8,078	5,587	4,317	1,551
Other Income (expense), Net	439	155	314	(74)	193
Income from Continuing Operations Before Income Taxes (1)	7,244	8,233	5,901	4,243	1,744
Income Tax Expense	1,728	2,866	1,618	1,558	325
Income from Continuing Operations	5,516	5,367	4,283	2,685	1,419
Net Loss from Discontinued Operations	(1,046)	(604)	(1,565)	(349)	(706)
Net Income (1)	\$4,470	\$4,763	\$2,718	\$2,336	\$713

Basic Net Income (loss) Per Share (1)

Continuing Operations	\$.64	\$.65	\$.52	\$.33	\$.18
Discontinued Operations	(.12)	(.07)	(.19)	(.05)	(.09)
	.52	.58	.33	.28	.09

Diluted Net Income (loss) Per Share (1)

Continuing Operations	\$.63	\$.64	\$.52	\$.33	\$.18
Discontinued Operations	(.12)	(.07)	(.19)	(.05)	(.09)
	.51	.57	.33	.28	.09

Cash Dividends Per Share	\$.27	\$.24	\$.21	\$.04	\$.30
Average Dilutive Shares Outstanding	8,716	8,263	8,186	8,246	8,365

Selected Balance Sheet Data

Total Assets	\$92,883	\$89,481	\$79,096	\$88,758	\$88,012
Property, Plant and Equipment, Net	7,691	6,289	4,871	6,369	7,021
Stockholders' Equity	79,851	77,051	70,840	68,871	67,308

(1) 2005, 2004 and 2003 amounts benefited from the implementation of Financial Accounting Standards No.142, Goodwill and Other Intangible Assets as disclosed in Note 9 of the consolidated financial statements, included in Item 8, because goodwill was not amortized in those periods.

Cautionary Statement: This annual report contains forward-looking statements concerning possible or anticipated future financial performance, business activities or plans which are typically preceded by the words "believes," "expects," "anticipates," "intends" or similar expressions. For such forward-looking statements, the Company claims the protection of the safe harbor for forward-looking statements contained in federal securities laws. Shareholders and the investing public should understand that such forward-looking statements are subject to risks and uncertainties which could cause actual performance, activities or plans to differ significantly from those indicated in the forward-looking statements. Such risks and uncertainties include, but are not limited to: lower sales to RBOC's and other major customers; competitive products and technologies; our ability to successfully reduce operating expenses at certain business units; the general health of the telecom sector; profitability of recent acquisitions; delays in new product introductions; higher than expected expense related to new sales and marketing initiatives; availability of adequate supplies of raw materials and components; fuel prices; and other factors discussed from time to time in the Company's filings with the Securities and Exchange Commission.

UNAUDITED QUARTERLY OPERATING RESULTS

(in thousands, except per share amounts)

2005	March 31	June 30	Sept. 30	Dec. 31
Sales from Continuing Operations	\$25,383	\$27,204	\$30,108	\$27,013
Gross Margins	8,945	8,729	10,576	8,620
Operating Income from Continuing Operations	1,581	925	3,216	1,083
Net Income	895	309	1,777	1,488
Basic Net Income per Share	\$.10	\$.04	\$.20	\$.18
Diluted Net Income per Share	\$.10	\$.04	\$.20	\$.17

2004	March 31	June 30	Sept. 30	Dec. 31
Sales from Continuing Operations	\$22,507	\$24,434	\$26,677	\$26,908
Gross Margins	7,585	8,596	9,548	9,605
Operating Income from Continuing Operations	2,349	1,103	1,856	2,771
Net Income	724	990	1,538	1,511
Basic Net Income per Share	\$.09	\$.12	\$.19	\$.18
Diluted Net Income per Share	\$.09	\$.12	\$.19	\$.17

COMMON STOCK INFORMATION

The Company's common stock is traded on the American Stock Exchange ("AMEX") under the trading symbol JCS.

The table below presents the range of high and low trading prices for the Company's stock for 2005 and 2004 as reported by AMEX.

Quarter	2005		2004	
	High	Low	High	Low
First	\$13.60	\$10.07	\$8.97	\$7.75
Second	11.79	8.65	9.24	7.66
Third	12.50	9.50	8.40	7.55
Fourth	12.40	9.48	12.74	8.25

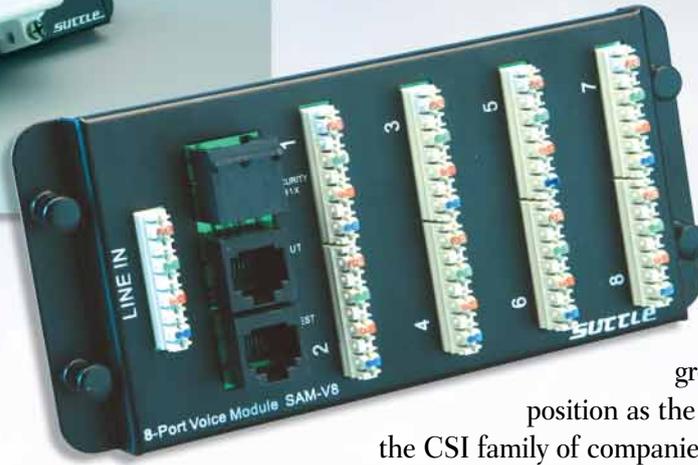
Information as filed with the Securities and Exchange Commission on Form 10-K is included in the pocket of this report.

DIVIDEND INCREASES

CSI continued its plan to increase dividends as the Board declared a cash dividend of \$.06 paid 1/3/05, \$.07 paid 4/1/05, 7/1/05 and 10/1/05; and \$.08 paid 1/1/06. At the Board meeting held March 2, 2006 a dividend of \$.08 per share was declared for payment on 4/1/06.



SUTTLE



Suttle manufactures telecommunications connection products and filtering devices for voice, data, and video applications. With a strong focus on market diversification and new product development, Suttle achieved substantial growth in 2005 and maintained its position as the leader in revenue and profits for the CSI family of companies.

Exciting changes are underway in the telecommunications industry that continues to provide Suttle with many opportunities. As service providers invest substantial capital into enhanced Voice /Data /Video “Triple Play” architectures, Suttle is well positioned as a trusted vendor to bring customer premise equipment solutions to these network builds. In addition to domestic service provider and distribution customers, Suttle continues to see significant growth with home builders and residential network installers as well as international service providers.

SOHO Access™

Suttle continues to execute on its plan to be a leading supplier of structured cabling solutions for the home. Structured wiring systems simplify and enhance a homebuyer’s lifestyle and create long-term value for the home. Ideal for FTTP (fiber to the premise), networks, Suttle’s SOHO Access™ (small office, home office), products provide an attractive, installer friendly and cost effective solution which has been well received by the marketplace. The end of 2005 saw the award of two key supply contracts for the SOHO Access™ family of products paving the way for a continued growth in 2006 and beyond.



DSL Line Conditioners™

DSL filtering products returned as the revenue leader for Suttle in 2005 with continued key wins for supply contracts. Renewed focus on efficient designs, best-cost manufacturing, and forward thinking supply chain management allows Suttle to remain a strong player in this very competitive market.

Core Business

Suttle’s core business of traditional phone connecting blocks, including the CorroShield™ line of corrosion resistant jacks, continues to hold a place of strength in the marketplace. The competitive voice business between service providers and the development of new technologies such as VoIP have created new markets for Suttle’s core products as well as product line extensions such as the Dual Provider Switch Products™.



David McGraw
President and General Manager



In 2005 Transition Networks introduced new products to strengthen its position as the leader in the media conversion technology space and undertook a major integration with a sister company to help diversify its product portfolio and provide more operational efficiencies for the Communications Systems Inc. stakeholders.

Early in the year Transition Networks introduced an industry first 10/100/1000AH product for the Ethernet in the first mile standard. For the coming year Transition Networks will increase its pace of introducing new products that target the core markets of enterprise and service providers as well as new products for new markets such as industrial and video.

Communications Systems Inc. announced in November 2005 that Transition Networks and MiLAN Technology were consolidating operations under the direction of Transition Networks' management. Since then, the two companies have been working to create one company with two industry leading brands. Transition Networks, the industry leader in media conversion technology, combined MiLAN, a network connectivity hardware provider, to form one network solutions hardware manufacturer offering media converters, fiber network interface cards, switch and wireless products.

To take Transition Networks' full solutions to market, the company has combined sales forces from both companies into one stronger sales force with a broader portfolio of products to offer. Leveraging the relationships with two distinct customer bases and distribution channels, Transition Networks can now penetrate further with more products and solutions with the cross pollination of product lines.

Transition Networks has gained efficiencies by managing both brands of products. As of January 1st, 2006 all Human Resources, Manufacturing, Planning, and Marketing will be based out of Eden Prairie and Minnetonka, Minnesota where Transition Networks is currently headquartered. By incorporating these functions and bringing them to Minnesota, the company has already lowered the cost to market for the MiLAN brand of products. Customer service, sales, and technical support functions will be maintained in the Sunnyvale, California location. The combination of a strong product roadmap and the efficiencies realized by the integration of MiLAN into Transition Networks positions the company to be the largest revenue producer in the Communication Systems Inc. portfolio in 2006.



Daniel G. Easter
President and General Manager





TECHNOLOGIES



Thomas J. Lapping
President and General Manager

JDL Technologies continues to demonstrate its expertise in deploying and managing end-to-end network services to insure security, reliability and availability of Information Technology (IT) resources. In keeping with its strategic focus, 2005 performance demonstrates that JDL is growing as an IT services company in the K-12 vertical market. This focus was rewarded in 2005 with new services revenue contracts from JDL's largest customers.

The nation's largest K-12 internal WiFi network is a product of JDL expertise in 2005. Broward County Schools, FL now connects 46,000 laptop computers to network and Internet resources. The central management of these highly secure wireless resources originates from the district network operations center, another service provided by JDL. This wireless system uses the Light Weight Access Point Protocol which adapts in real time to changing RF (radio frequencies), environments and external interference by changing frequency channels and load balancing traffic across multiple access points to improve network performance. JDL effectively and efficiently manages this wireless network system without a large staff and without a need to roll trucks to solve problems.

In 2006, an even higher percentage of JDL's overall business will come from the higher-margin IT services category. JDL will deploy a new microwave network expansion for the US Virgin Islands Department of Education to provide voice, video and data services to its schools. JDL has also secured a three-year contract to implement and support remote computer management services to more than 100,000 workstations and laptops in the School Board of Broward County, FL. Desktop computer management is a new offering from JDL that will expand on services for managing triple play networks.

JDL's focus on next generation technologies and how they can be integrated into the K-12 market continues to position the company for future growth. JDL has differentiated itself in the K-12 vertical market with a solution to deliver video over the IP network. Live, prerecorded or on-demand video resources are delivered over a private enterprise switched Ethernet network. Network delivery of video enables triple play convergence in the K-12 market by providing video to teacher's desktops for classroom projection and to students from any computer or television end point device on the network. JDL deployed this system to deliver both on-demand video and 23 stations of video in the Lower Merion School District, PA.

JDL's professional development and training services also expanded in 2005 from the New York City Board of Education to the Dallas, TX and Clark County School District in Las Vegas, Nevada as well as in several districts in Minnesota. This offering uses existing curriculum to integrate technology into the teaching practice by training teachers and students together to create project-based and inquiry-based learning environments.

The continuing growth in the use of IT services in the K-12 enterprise is also JDL's opportunity for growth. JDL promises innovative technical solutions that enable the success of students, teachers and school districts by increasing the value and reliability of the services delivered by IT.

BOARD OF DIRECTORS

Curtis A. Sampson	Chairman and Chief Executive Officer
Paul J. Anderson	Private Investor
Edwin C. Freeman	Vice President and General Manager, Bro-tex, Inc.
Luella Gross Goldberg	Director of several corporations
Frederick M. Green	Retired President and Chief Executive Officer, Ault Incorporated
Gerald D. Pint	Retired Vice President, Telecom Systems, Group, 3M Company
Randall D. Sampson	President and Chief Executive Officer Canterbury Park Holding Corporation
Wayne E. Sampson	Private Investor

Compensation Committee

Gerald Pint, Luella G. Goldberg and Fred Green

Governance and Nominating Committee

Luella G. Goldberg, Gerald Pint and Paul Anderson

Finance Committee

Curtis Sampson, Paul Hanson, Wayne Sampson, Randy Sampson and Edwin Freeman.

Audit Committee

Luella G. Goldberg, Edwin Freeman and Paul Anderson

OFFICERS

Curtis A. Sampson*	Chairman and Chief Executive Officer
Jeffrey K. Berg*	President and Chief Operating Officer
Paul N. Hanson*	Chief Financial Officer, Vice President of Finance, Treasurer and Secretary
Daniel G. Easter	President and General Manager Transition Networks, Inc.
Thomas J. Lapping	President and General Manager, JDL Technologies, Inc.
David T. McGraw	President and General Manager, Suttle
Brian R. Lucker	Controller
Michael J. Skucius	Director of Information Services
Karen J. Nesburg Bleick	Director of Human Resources
* Corporate Officer	

LEGAL COUNSEL

Richard A. Primuth Lindquist & Vennum P.L.L.P.

Special Thank You

Frederick M. Green has chosen not to seek re-election to the CSI Board as he recently retired as President & CEO of Ault, Inc. and is relocating to the East Coast. We would like to thank Fred for his 10 years of service as a director of CSI.

CSI Board of Directors. Seated, left to right: Curtis A. Sampson, Luella Goldberg and Gerald Pint. Standing, left to right: Wayne Sampson, Randall Sampson, Fred Green, Paul Anderson, and Edwin Freeman



CORPORATE INFORMATION

Corporate Headquarters
Communications Systems, Inc.
213 South Main Street
Hector, Minnesota 55342
320-848-6231

Transfer Agent and Registrar
Wells Fargo Bank, N.A.
South St. Paul, Minnesota

Independent Auditor
Deloitte & Touche LLP
Minneapolis, Minnesota

Corporate Counsel
Lindquist & Vennum P.L.L.P.
Minneapolis, Minnesota

The Company maintains a website at www.commsystems.com. Our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our periodic reports on Form 8-K (and any amendments to these reports) are available free of charge by linking from our website to the Securities & Exchange Commission website.

ANNUAL MEETING

The annual meeting of shareholders will be held on Thursday, May 25, 2006 at 3:00 p.m. at the offices of Communications Systems, Inc., 6475 City West Parkway, Eden Prairie, MN.

CSI Communications Systems, Inc.

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www.commsystems.com*