

Edgar Filing: KRONOS INC - Form 10-Q

KRONOS INC  
Form 10-Q  
August 08, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 28, 2003

OR

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

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

Commission file number 0-20109

-----  
Kronos Incorporated  
-----

(Exact name of registrant as specified in its charter)

Massachusetts

04-2640942

-----  
(State or other jurisdiction of  
incorporation or organization)

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

297 Billerica Road, Chelmsford, MA 01824

-----  
(Address of principal executive offices) (Zip Code)

(978) 250-9800

-----  
(Registrant's telephone number, including area code)

-----  
(Former name, former address and former fiscal year, if changed  
since last report)

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

Yes X No  
-----

Indicate by check mark whether the registrant is an accelerated filer (as  
defined in Rule 12b-2 of the Exchange Act).

Yes X No  
-----

As of August 1, 2003, 20,177,589 shares of the registrant's common stock,  
\$.01 par value, were outstanding.

# Edgar Filing: KRONOS INC - Form 10-Q

## KRONOS INCORPORATED

### INDEX

PART I. FINANCIAL INFORMATION	Page
-----	
Item 1. Condensed Consolidated Financial Statements (Unaudited)	
Condensed Consolidated Statements of Income for the Three and Nine Months Ended June 28, 2003 and June 29, 2002	1
Condensed Consolidated Balance Sheets at June 28, 2003 and September 30, 2002	2
Condensed Consolidated Statements of Cash Flows for the Nine Months Ended June 28, 2003 and June 29, 2002	3
Notes to Condensed Consolidated Financial Statements	4
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	16
Item 3. Quantitative and Qualitative Disclosure About Market Risk	31
Item 4. Evaluation of Disclosure Controls and Procedures	32
PART II. OTHER INFORMATION	
Item 6. Exhibits and Reports on Form 8-K	33
Signatures	

## PART I. FINANCIAL INFORMATION

### Item 1. Condensed Consolidated Financial Statements (Unaudited)

KRONOS INCORPORATED  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
(In thousands, except share and per share amounts)  
UNAUDITED

	Three Months Ended		N
	June 28, 2003	June 29, 2002	June 20
Net revenues:			
Product .....	\$ 42,185	\$ 40,458	\$ 12
Maintenance .....	32,826	27,104	9
Professional services .....	23,205	19,508	6
	98,216	87,070	28
Cost of sales:			

Edgar Filing: KRONOS INC - Form 10-Q

Costs of product .....	10,097	10,106	3
Costs of maintenance and professional services	28,156	24,770	8
	-----	-----	-----
	38,253	34,876	11
	-----	-----	-----
Gross profit .....	59,963	52,194	17
Operating expenses and other income:			
Sales and marketing .....	31,052	28,337	9
Engineering, research and development .....	9,894	9,023	2
General and administrative .....	6,063	5,507	1
Amortization of intangible assets .....	985	746	
Other income, net .....	(1,384)	(1,378)	(
	-----	-----	-----
	46,610	42,235	13
	-----	-----	-----
Income before income taxes .....	13,353	9,959	3
Provision for income taxes .....	4,969	3,462	1
	-----	-----	-----
Net income .....	\$ 8,384	\$ 6,497	\$ 2
	=====	=====	=====
Net income per common share:			
Basic .....	\$ 0.42	\$ 0.33	\$
	=====	=====	=====
Diluted .....	\$ 0.41	\$ 0.32	\$
	=====	=====	=====
Weighted-average common shares outstanding:			
Basic .....	19,885,619	19,658,011	19,79
	=====	=====	=====
Diluted .....	20,655,010	20,349,674	20,54
	=====	=====	=====

See accompanying notes to condensed consolidated financial statements.

KRONOS INCORPORATED  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (In thousands, except share and per share amounts)  
 UNAUDITED

ASSETS

Current assets:

Cash and equivalents .....	\$
Marketable securities .....	
Accounts receivable, less allowances of \$7,831 .....	
at June 28, 2003 and \$9,697 at September 30, 2002	
Deferred income taxes .....	

Edgar Filing: KRONOS INC - Form 10-Q

Other current assets .....	
Total current assets .....	
Property, plant and equipment, net .....	
Marketable securities .....	
Intangible assets .....	
Goodwill .....	
Capitalized software, net .....	
Other assets .....	
Total assets .....	\$

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:	
Accounts payable .....	\$
Accrued compensation .....	
Accrued expenses and other current liabilities .....	
Deferred product revenues .....	
Deferred professional service revenues .....	
Deferred maintenance revenues .....	
Total current liabilities .....	
Deferred maintenance revenues .....	
Deferred income taxes .....	
Other liabilities .....	
Shareholders' equity:	
Preferred Stock, par value \$1.00 per share: authorized 1,000,000 shares, no shares issued and outstanding .....	
Common Stock, par value \$.01 per share: authorized 50,000,000 shares, 20,032,082 and 19,911,952 shares issued at June 28, 2003 and September 30, 2002, respectively .	
Additional paid-in capital .....	
Retained earnings .....	
Cost of Treasury Stock (173 shares and 366,062 shares at June 28, 2003 and September 30, 2002, respectively) .....	
Accumulated other comprehensive loss:	
Foreign currency translation .....	
Net unrealized (loss)/gain on available-for-sale investments .....	
Total shareholders' equity .....	
Total liabilities and shareholders' equity .....	\$

See accompanying notes to condensed consolidated financial statements.

KRONOS INCORPORATED  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)  
UNAUDITED

Edgar Filing: KRONOS INC - Form 10-Q

	Nine M ----- June 28, 2003 -----
Operating activities:	
Net income .....	\$ 22,695
Adjustments to reconcile net income to net cash and equivalents provided by operating activities:	
Depreciation .....	8,100
Amortization of intangible assets .....	2,537
Amortization of capitalized software .....	8,624
Provision for deferred income taxes .....	601
Changes in certain operating assets and liabilities:	
Accounts receivable, net .....	10,015
Deferred product revenues .....	(2,889)
Deferred professional service revenues .....	(399)
Deferred maintenance revenues .....	879
Accounts payable, accrued compensation and other liabilities .....	(3,278)
Taxes payable .....	(27)
Other .....	(409)
Tax benefit from exercise of stock options .....	6,760
	-----
Net cash and equivalents provided by operating activities .....	53,209
Investing activities:	
Purchase of property, plant and equipment .....	(8,452)
Capitalized internal software development costs .....	(8,982)
Increase in marketable securities .....	(17,889)
Acquisitions of businesses and software, net of cash acquired .....	(13,245)
	-----
Net cash and equivalents used in investing activities .....	(48,568)
Financing activities:	
Net proceeds from exercise of stock options and employee purchase plans .....	16,929
Purchase of treasury stock .....	(14,704)
Proceeds from (net investment in) call options .....	2,596
	-----
Net cash and equivalents provided by/(used in) financing activities .....	4,821
Effect of exchange rate changes on cash and equivalents .....	979
	-----
Increase (decrease) in cash and equivalents .....	10,441
Cash and equivalents at the beginning of the period .....	34,117
	-----
Cash and equivalents at the end of the period .....	\$ 44,558
	=====

See accompanying notes to condensed consolidated financial statements.

KRONOS INCORPORATED  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE A - General

## Edgar Filing: KRONOS INC - Form 10-Q

The accompanying unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring accruals that management of Kronos Incorporated (the "Company" or "Kronos") considers necessary for a fair presentation of the Company's financial position and results of operations as of and for the interim periods presented pursuant to the rules and regulations of the Securities and Exchange Commission. Certain footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes the disclosures in these financial statements are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the Company's audited financial statements for the fiscal year ended September 30, 2002. The results of operations for the three and nine months ended June 28, 2003 are not necessarily indicative of the results for a full fiscal year. Certain reclassifications have been made in the accompanying consolidated financial statements in order to conform to the fiscal 2003 presentation.

### NOTE B - Fiscal Quarters

The Company utilizes a system of fiscal quarters. Under this system, the first three quarters of each fiscal year end on a Saturday. However, the fourth quarter of each fiscal year will always end on September 30. Because of this, the number of days in the first quarter (89 days in fiscal 2003 and 90 days in fiscal 2002) and fourth quarter (94 days in fiscal 2003 and 93 days in fiscal 2002) of each fiscal year varies from year to year. The second and third quarters of each fiscal year will be exactly thirteen weeks long. This policy does not have a material effect on the comparability of results of operations between quarters.

### NOTE C - Other Current Assets

Other current assets consists of the following (in thousands):

	June 28, 2003 -----	September 30, 2002 -----
Inventory	\$ 6,303	\$ 6,492
Prepaid expenses	12,862	11,343
	-----	-----
Total	\$19,165 =====	\$17,835 =====

### NOTE D - Intangible Assets

Acquired intangible assets subject to amortization are presented in the following table (in thousands).

As of June 28, 2003:

	Weighted Average Life in Years -----	Gross Carrying Value -----	Accumulated Amortization -----

Edgar Filing: KRONOS INC - Form 10-Q

Intangible assets:			
Customer related .....	9.8	\$22,084	\$ 8,693
Maintenance relationships	11.9	9,091	910
Tax benefits .....	10.7	2,142	473
Non-compete agreements ..	4.2	3,353	1,582
		-----	-----
Total intangible assets .....		\$36,670	\$11,658
		=====	=====

As of September 30, 2002:

Intangible assets:			
Customer related .....	9.5	\$19,166	\$ 6,851
Maintenance relationships	11.9	6,267	535
Tax benefits .....	10.7	2,127	309
Non-compete agreements ..	5.1	1,908	1,228
		-----	-----
Total intangible assets .....		\$29,468	\$ 8,923
		=====	=====

For the three months ended June 28, 2003 and June 29, 2002, the amount of acquired goodwill is \$2.7 million and \$0.3 million, respectively. The amount of goodwill acquired during the nine months ended June 28, 2003 and June 29, 2002 is \$12.3 million and \$21.8 million, respectively.

For the three and nine months ended June 28, 2003, the Company recorded amortization expense for intangible assets of \$1.0 million and \$2.5 million, respectively. The estimated annual amortization expense for intangible assets for the current and next five fiscal years is as follows (in thousands):

Fiscal Year Ending September 30, -----	Estimated Annual Amortization Expense -----
2003	\$3,524
2004	3,678
2005	3,176
2006	2,888
2007	2,638
2008	2,531

NOTE E - Acquisitions

On May 16, 2003, the Company completed the acquisition of the Abra Enterprise customer base from Best Software. The aggregate purchase price was not material to the Company's financial position. The results of operations related to the purchase of these customers, which is not material to the Company's results of operations, has been included in the consolidated financial statements since that date. As a result of the acquisition, the Company gained access to the

## Edgar Filing: KRONOS INC - Form 10-Q

existing Abra Enterprise customers through its direct sales and service organizations, which broadens the Company's presence in the Human Resource Management Systems market. In addition, the Company gained access to the existing maintenance revenue stream from these customers. The deferred revenue related to the maintenance revenue stream, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as described in EITF 01-03.

On May 6, 2003, the Company completed the acquisition of certain assets of Simplex International Pty Ltd. ("Simplex International"). Based in Australia, Simplex International was engaged in the marketing, selling, supporting and maintaining integrated workforce management software solutions. The aggregate purchase price was not material to the Company's financial position. The results of Simplex International's operations, which are not material to the Company's results of operations, have been included in the consolidated financial statements since that date. As a result of the acquisition, the Company expects to increase its presence in the mid-market sector in Australia, through its subsidiary in Australia, Kronos Australia Pty. Ltd. The mid market sector includes companies with between 250 and 1,000 employees. In connection with the acquisition, the Company assumed obligations to provide services associated with maintenance contracts and obligations to provide professional services, primarily installation services. The deferred revenue related to the maintenance and professional services revenue streams, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as described in EITF 01-03.

On March 11, 2003, the Company completed the acquisition of certain assets of Ban-koe Systems, Inc. ("BKS"), the former Minnesota-based Kronos dealer. The aggregate purchase price was not material to the Company's financial position. The results of BKS's operations, which are not material to the Company's results of operations, have been included in the consolidated financial statements since that date. BKS was engaged in the sale and service of employee time and attendance, employee scheduling, data collection and labor management hardware and software systems, including the resale of the Company's products through a dealer relationship. As a result of the acquisition, the Company gained access to existing and prospective customers in several states (including Michigan, Illinois, Iowa, Wisconsin, and Minnesota) through its direct sales and service organizations, as well as access to the existing maintenance revenue stream from BKS customers. The deferred revenue related to the maintenance revenue stream, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as described in EITF 01-03. Due to the significant volume of customer maintenance support contracts assumed in conjunction with the BKS acquisition, the Company has not finalized the allocation of the purchase price. The Company anticipates that the allocation of the purchase price will be completed by September 30, 2003.

On January 20, 2003, the Company completed the acquisition of the maintenance agreements of DataPro Solutions, Inc. ("DP"), the former Washington state-based Kronos dealer. The aggregate purchase price was not material to the Company's financial position. The results of DP operations, which are not material to the Company's results of operations, have been included in the consolidated financial statements since that date. DP was engaged in the sale and service of employee time and attendance, employee scheduling, data collection and labor management hardware and software systems, including the resale of the Company's products through a dealer relationship. As a result of the acquisition, the Company gained access to the existing maintenance revenue stream from DP customers. The deferred revenue related to the maintenance revenue stream, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as



## Edgar Filing: KRONOS INC - Form 10-Q

described in EITF 01-03.

On November 20, 2002, the Company completed the acquisition of certain assets and the ongoing business operations of Hi-Tek Special Systems, Inc. ("HT"), the former Texas-based Kronos dealer. The aggregate purchase price was not material to the Company's financial position. The results of HT's operations, which are not material to the Company's results of operations, have been included in the consolidated financial statements since that date. HT was engaged in the sale and service of employee time and attendance, employee scheduling, data collection and labor management hardware and software systems, including the resale of the Company's products through a dealer relationship. As a result of the acquisition, the Company gained access to existing and prospective customers in the Texas, New Mexico and Mexico area through its direct sales and service organizations, as well as access to the existing maintenance revenue stream from HT customers. The deferred revenue related to the maintenance revenue stream, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as described in EITF 01-03.

On December 28, 2001, the Company completed the acquisition of certain assets and the ongoing business operations of the Integrated Software Business of SimplexGrinnell's Workforce Solutions Division ("SimplexGrinnell"). The aggregate purchase price was \$22.1 million in cash. The results of SimplexGrinnell's operations have been included in the consolidated financial statements since that date. SimplexGrinnell was engaged in the development, sales and support of integrated workforce management software solutions. As a result of the acquisition, the Company has increased its presence in the mid-market sector, which includes companies with between 250 and 1,000 employees.

The SimplexGrinnell transaction was accounted for under the purchase method of accounting and accordingly, the assets and liabilities acquired were recorded at their estimated fair values at the effective date of the acquisition. The goodwill recognized is deductible for income tax purposes. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition (in thousands).

	At December 28, 2001
	-----
Accounts receivable	\$ 6,678
Customer related intangible asset (amortized over 12 years)	1,100
Maintenance relationships intangible asset (amortized over 12 years)	2,500
Goodwill	17,933
Other assets	768
	-----
Total assets acquired	28,979
Deferred professional services revenue	(1,564)
Deferred maintenance revenue	(5,025)
Other liabilities	(340)
	-----
Total liabilities assumed	(6,929)
	-----
Net assets acquired	\$22,050
	=====

## Edgar Filing: KRONOS INC - Form 10-Q

In connection with the acquisition of the assets and liabilities of SimplexGrinnell in December 2001, the Company acquired obligations to provide services associated with maintenance contracts and obligations to provide professional services, primarily installation services. The amounts of deferred revenue ascribed to acquired maintenance obligations and professional services amounts to \$5.0 million and \$1.6 million, respectively. The deferred revenue, which was recorded at an amount approximating cost, plus a normal profit margin, was recognized as the Company had assumed a legal performance obligation as described in EITF 01-03. The acquired maintenance arrangements required the Company to provide phone support, bug fixes and unspecified upgrades for the remaining contract terms. The acquired professional services obligations required the Company to provide installation services.

Certain agreements contain provisions that require the Company to make a guaranteed payment and/or contingent payments based upon profitability of the business unit or if specified minimum revenue requirements are met. These provisions expire during fiscal 2003 through 2006. Guaranteed payments are accrued at the time of the acquisition and are included in the purchase price allocation. Contingent payments due under the terms of the agreements are recognized when earned and are principally recorded as goodwill. However, under certain circumstances, a portion of the contingent payment may be recorded as compensation expense. There were no contingent payments earned during the three months ended June 28, 2003 and June 29, 2002. During the first nine months of fiscal 2003 and 2002, \$1.8 million and \$0.8 million, respectively, of contingent payments were earned, all of which were recorded as goodwill. There are several contingent payment arrangements currently outstanding, on which the Company may have future payment obligations, contingent upon the achievement of various financial performance goals. As of June 28, 2003, the Company has the obligation to pay \$5.1 million in guaranteed payments. These payments will be made at various dates through fiscal 2006.

### NOTE F - Comprehensive Income

For the three and nine months ended June 28, 2003 and June 29, 2002, comprehensive income consisted of the following (in thousands):

	Three Months Ended		Nine Months Ended	
	June 28, 2003	June 29, 2002	June 28, 2003	June 29, 2002
Comprehensive income:				
Net income .....	\$ 8,384	\$ 6,497	\$ 22,695	\$ 18,400
Cumulative translation adjustment	923	298	1,383	600
Unrealized (loss)/gain on available-for-sale securities ...	(70)	220	(340)	(200)
Total comprehensive income .....	\$ 9,237	\$ 7,015	\$ 23,738	\$ 18,800

### NOTE G - Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except share and per share data):

Edgar Filing: KRONOS INC - Form 10-Q

	Three Months Ended		Nine Mo
	June 28, 2003	June 29, 2002	June 28, 2003
Net income .....	\$ 8,384	\$ 6,497	\$ 22,695
Weighted-average shares .....	19,885,619	19,658,011	19,792,994
Effect of dilutive securities:			
Employee stock options .....	769,391	691,663	747,130
Adjusted weighted-average shares and assumed conversions .....	20,655,010	20,349,674	20,540,124
Basic earnings per share .....	\$ .42	\$ 0.33	\$ 1.15
Diluted earnings per share .....	\$ .41	\$ 0.32	\$ 1.10

NOTE H - New Accounting Pronouncements

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123." This statement provides alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based compensation. The statement amends the disclosure requirements of FASB Statement No. 123 to require prominent disclosure in both annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. The Company accounts for stock-based compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure provisions of FASB Statement No. 123. The transition provisions are effective for fiscal years ending after December 15, 2002. The disclosure provisions are effective for interim periods beginning after December 15, 2002. The Company has implemented the required disclosure provisions in the three month period ending March 29, 2003. The adoption of this statement is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows as the Company does not anticipate making the voluntary change to the fair value method of accounting for stock-based compensation.

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities, an interpretation of Accounting Research Bulletin No. 51." FIN No. 46 requires certain variable interest entities, or VIEs, to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN No. 46 is effective for all VIEs created or acquired after January 31, 2003. For VIEs created or acquired prior to February 1, 2003, the provisions of FIN No. 46 must be applied for the first interim or annual period beginning after June 15, 2003.

## Edgar Filing: KRONOS INC - Form 10-Q

The Company currently has no contractual relationship or other business relationship with a variable interest entity and therefore the adoption of FIN No. 46 did not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

### NOTE I - Call Option Arrangements

The Company periodically enters into call option arrangements, which are classified as an equity instrument in accordance with the provisions of EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." During the nine month period ended June 28, 2003, a call option arrangement matured in December 2002. At maturity, the Company's stock price exceeded the strike price of \$25.00 per share and the Company received a return of its cash investment and a premium totaling approximately \$2.6 million, which is credited to additional paid-in-capital. If at maturity the Company's stock price was less than the strike price, the Company would use its cash investment to purchase Company shares at a predetermined price. A call option arrangement provides the Company an opportunity to lock in a repurchase price for shares under the Company's stock repurchase program. There are no dividend and liquidation preferences, participation rights, sinking-fund requirements, unusual voting rights or any other significant terms pertaining to these call option arrangements. As of June 28, 2003, the Company did not have any call option arrangements outstanding.

### NOTE J - Stock-Based Compensation

The Company accounts for its stock-based compensation plan under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" to stock-based employee compensation (in thousands, except per share data).

	Three Months Ended		Nine Months Ended	
	June 28, 2003	June 29, 2002	June 28, 2003	June 29, 2002
Net income, as reported .....	\$8,384	\$6,497	\$22,695	\$ 18,467
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(1,522)	(1,287)	(5,652)	(5,322)
Pro forma net income .....	\$6,862	\$5,210	\$17,043	\$ 13,145
Earnings per share:				
Basic--as reported .....	\$ 0.42	\$ 0.33	\$ 1.15	\$ 0.94

Edgar Filing: KRONOS INC - Form 10-Q

Basic--pro forma .....	\$ 0.35 =====	\$ 0.27 =====	\$ 0.86 =====	\$ 0.67 =====
Diluted--as reported .....	\$ 0.41 =====	\$ 0.32 =====	\$ 1.10 =====	\$ 0.90 =====
Diluted--pro forma .....	\$ 0.33 =====	\$ 0.26 =====	\$ 0.83 =====	\$ 0.64 =====

NOTE K - Additional Stock Option Program Information

Option Program Description: The Company intends that its stock option program be its primary vehicle for offering long-term incentives and rewarding its executives and key employees. Stock options are granted to key employees based upon, among other things, prior performance of the executive or key employee, the importance of retaining their services for the Company and the potential for their performance to help the Company attain its long-term goals. There is no set formula for the award of options to individual executives or employees.

Stock options are generally granted annually in conjunction with the Compensation Committee's formal review of the individual performance of its key executives, including its Chief Executive Officer, and their contributions to the Company. In the nine month period ended June 28, 2003, 76% of the options granted went to employees other than the Named Executive Officers. The Named Executive Officers for the first nine month period of fiscal 2003 and for fiscal 2002, for purposes of this footnote, are the same Named Executive Officers for fiscal 2002, which are identified in the Company's definitive proxy statement for the 2003 Annual Meeting of Stockholders. The Named Executive Officers for fiscal 2001 are the officers which are identified in the Company's definitive proxy statement for the 2002 Annual Meeting of Stockholders. All the options awarded are granted from the same plan. Options, which are granted at the fair market value on the date of grant, typically vest annually over a four-year period beginning one year from the date of grant and have a contractual life of four years and six months.

Distribution and Dilutive Effect of Options:

Employee and Named Executive Officer Option Grants:

	For the Nine Month Period Ended June 28, 2003 -----	For the Fiscal Year Ended September 30, 2002 -----	For the Fis Year Ended September 3 2001 -----
Net grants during period as % of outstanding ... shares	4.1%	4.7%	4.2%
Grants to Named Executive Officers during period as % of options granted	24.1%	25.3%	17.0%
Grants to Named Executive Officers ..... during period as % of shares outstanding	1.0%	1.2%	0.7%

Edgar Filing: KRONOS INC - Form 10-Q

General Option Information:

Summary of Option Activity  
(in thousands, except per share data)

	Shares Available for Options	Number of Option Shares Outstanding	Weighted-Average Exercise Price per Share
Outstanding at September 30, 2002	1,624	2,641	\$ 23.18
Grants .....	(828)	828	25.36
Exercises .....	--	(770)	18.51
Cancellations ....	10	(71)	24.12
Outstanding at June 28, 2003 ....	806	2,628	\$ 25.21

In-the-Money and Out-of-the-Money Option Information as of June 28, 2003  
(in thousands, except per share data)

	Exercisable		Unexercisable	
	Shares	Weighted-Average Exercise Price per Share	Shares	Weighted-Average Exercise Price per Share
In-the-Money .....	594	\$ 24.52	2,034	\$ 25.41
Out-of-the-Money (1) ....	--	--	--	--
Total Options Outstanding	594	\$ 24.52	2,034	\$ 25.41

(1) Out-of-the-Money options are those options with an exercise price equal to or above the closing price of \$49.19 at the end of the current quarter.

Executive Options: The following tables summarize option grants and exercises during the nine month period ended June 28, 2003 to the Company's Named Executive Officers and the value of the options held by such persons at June 28,

Edgar Filing: KRONOS INC - Form 10-Q

2003.

Options Granted to Named Executive Officers

-----

Name	Individual Grants				5%
	Number of Securities Underlying Options Granted (1)	Percent of Total Options Granted to Employees in Nine Month Period Ended June 28, 2003 (2)	Exercise or Base Price per Share (3)	Expiration Date	
Mark S. Ain ..... CEO & Chairman	60,000	7.2%	\$24.86	04/07/07	\$366,7
Paul A. Lacy ..... Exec. V.P. and Chief Financial & Administrative Officer	40,000	4.8%	24.86	04/07/07	244,5
Aron J. Ain ..... Exec. V.P. and Chief Operating Officer	40,000	4.8%	24.86	04/07/07	244,5
Peter C. George ..... V.P., Engineering & Chief Technology Officer	30,000	3.6%	24.86	04/07/07	183,3
James Kizielewicz ..... V.P., Marketing and Corporate Strategy	30,000	3.6%	24.86	04/07/07	183,3

- (1) Each option vests in four equal annual installments commencing one year from the date of grant.
- (2) Based on an aggregate of 828,400 shares subject to options granted to employees of the Company in the nine month period ended June 28, 2003.
- (3) The exercise price of each option was equal to the fair market value of the Company's common stock on the date of grant as reported by The NASDAQ National Market (R).
- (4) Amounts represent hypothetical gains that could be achieved for the respective options if exercised at the end of the option term. These gains are based on assumed rates of stock appreciation of 5% and 10% compounded annually from the date the respective options were granted to their expiration date (and are shown net of the option exercise price, but do not include deductions for taxes or other expenses associated with the exercise

## Edgar Filing: KRONOS INC - Form 10-Q

of the options or the sale of the underlying shares.) Actual gains, if any, on stock option exercises will depend on the future performance of the common stock, the optionholder's continued employment with the Company through the option vesting period and the date on which the options are exercised.

Option Exercises and Remaining Holdings of Named Executive Officers (for the nine month period ended June 28, 2003)

Name -----	Shares Acquired on Exercise -----	Value Realized (1) -----	Number of Securities Underlying Unexercised Options at June 28, 2003 -----
Mark S. Ain .....	67,500	\$1,890,675	96,000/153,000
Paul A. Lacy ....	51,750	1,307,691	27,750/98,500
Aron J. Ain .....	61,750	1,610,471	17,750/98,500
Peter C. George	17,250	459,189	36,000/73,500
James Kizielewicz	31,500	878,034	9,000/75,000

(1) Represents the difference between the exercise price and the fair market value of the common stock on the date of exercise.

(2) Based on the fair market value of the common stock on June 28, 2003 (\$49.19), the last day of the third quarter of the Company's 2003 fiscal year, less the option exercise price.

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

### Forward-Looking Statements

This discussion includes certain forward-looking statements about Kronos' business and its expectations, including statements relating to product and service revenues, revenue growth rates, operating expenses, gross profit, future acquisitions and available cash, investments and operating cash flow, Kronos' ability to obtain third-party financing, and the future effects of accounting pronouncements. Any such statements are subject to risk that could cause the actual results to vary materially from expectations. For a further discussion of the various risks that may affect Kronos' business and expectations, see "Certain Factors That May Affect Future Operating Results" in our Annual Report of Form 10-K for the fiscal year ended September 30, 2002 at the end of



## Edgar Filing: KRONOS INC - Form 10-Q

Management's Discussion and Analysis of Financial Condition and Results of Operations. The risks and uncertainties discussed herein and in our Annual Report on Form 10-K for the year ended September 30, 2002 do not reflect the potential future impact of any mergers, acquisitions or dispositions. In addition, any forward-looking statements represent our estimates only as of the day this Quarterly Report was filed with the Securities and Exchange Commission and should not be relied upon as representing our estimates as of any subsequent date. While we may elect to update forward-looking statements at some point in the future, we specifically disclaim any obligation to do so, even if our estimates change.

### Overview

Kronos is a single-source provider of human resources, payroll, scheduling, and time and labor solutions. Kronos' solutions are designed for a wide range of businesses from single-site to large multi-site enterprises. Kronos derives revenues from the licensing of its software solutions, sales of its hardware solutions and providing professional services as well as ongoing customer support and maintenance.

Management at Kronos believes that the continued economic environment may result in many customers deferring or reducing their technology purchases in the future. While management believes the impact on technology purchasing may be temporary, the effect may continue to cause delays or reductions in customer purchases of Kronos products and services in the future.

Regarding expectations for the remainder of the current fiscal year, management presently anticipates that revenue growth for the fourth quarter and for the entire fiscal 2003, including revenues from customers obtained in the acquisition of businesses, will range between 7% - 11% and 14% - 15%, respectively.

### Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations are based upon Kronos' consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires Kronos to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. Kronos bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from these estimates under different assumptions or conditions.

Kronos has identified the following critical accounting policies that affect the more significant judgments and estimates used in the preparation of consolidated financial statements. This listing is not a comprehensive list of all of Kronos' accounting policies. Please refer to Note A in the Notes to Consolidated Financial Statements in Item 15 of Kronos' Annual Report on Form 10-K for the fiscal year ended September 30, 2002 for further information.

Revenue Recognition - The Company licenses software and sells data collection hardware and related ancillary products to end-user customers through its direct sales force as well as indirect channel customers, Automatic Data Processing, Inc. ("ADP") and its independent resellers. Substantially all of the Company's software license revenue is earned from perpetual licenses of off-the-shelf software requiring no modification or customization. The software license, data collection hardware and related ancillary product revenues from the Company's end-user customers and indirect channel customers are generally

## Edgar Filing: KRONOS INC - Form 10-Q

recognized using the residual method when:

- o persuasive evidence of an arrangement exists, which is typically when a non-cancelable sales and software license agreement has been signed;
- o delivery, which is typically FOB shipping point, is complete for the software (either physically or electronically), data collection hardware and related ancillary products;
- o the customer's fee is deemed to be fixed or determinable and free of contingencies or significant uncertainties;
- o collectibility is probable; and
- o vendor specific objective evidence of fair value exists for all undelivered elements, typically maintenance and professional services.

Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and is recognized as revenue, assuming all other conditions for revenue recognition have been satisfied. Substantially all of the Company's product revenue is recognized in this manner. If the Company cannot determine the fair value of any undelivered element included in an arrangement, the Company will defer revenue until all elements are delivered, services are performed or until fair value can be objectively determined.

As part of an arrangement, end-user customers typically purchase maintenance contracts as well as professional services from the Company. Maintenance services include telephone and Web-based support as well as rights to unspecified upgrades and enhancements, when and if the Company makes them generally available. Professional services are deemed to be non-essential and typically are for implementation planning, loading of software, installation of the data collection hardware, training, building simple interfaces, running test data, and assisting in the development and documentation of pay rules and best practices consulting.

Revenues from maintenance services are recognized ratably over the term of the maintenance contract period based on vendor specific objective evidence of fair value. Vendor specific objective evidence of fair value is based upon the amount charged when purchased separately, which is typically the contract's renewal rate. Maintenance services are typically stated separately in an arrangement. The Company has classified the allocated fair value of revenues pertaining to the contractual maintenance obligations that exist for the 12-month period subsequent to the balance sheet date as a current liability, and the contractual obligations with a term beyond 12 months as a non-current liability. Revenues from time and material maintenance services are recognized as the services are delivered.

Revenues from professional services are generally recognized based on vendor specific objective evidence of fair value when: (1) a non-cancelable agreement for the services has been signed or a customer's purchase order has been received; and (2) the professional services have been delivered. Vendor specific objective evidence of fair value is based upon the price charged when these services are sold separately and are typically an hourly rate for professional services and a per class rate for training. Based upon the Company's experience in completing product implementations, it has determined that these services are typically delivered within a 12-month period subsequent to the contract signing and therefore classifies deferred professional services as a current liability.

The Company's arrangements with its end-user customers and indirect channel customers do not include any rights of return or price protection, nor do arrangements with indirect channel customers include any acceptance provisions. Generally, the Company's arrangements with end-user customers also do not

## Edgar Filing: KRONOS INC - Form 10-Q

include any acceptance provisions. However, if an arrangement does include acceptance provisions, they typically are based on the Company's standard acceptance provision. The Company's standard acceptance provision provides the end-user customer with a right to a refund if the arrangement is terminated because the product did not meet Kronos' published specifications. Generally, the Company determines that these acceptance provisions are not substantive and therefore should be accounted for as a warranty in accordance with SFAS No. 5.

At the time the Company enters into an arrangement, the Company assesses the probability of collection of the fee and the terms granted to the customer. For end-user customers, the Company's typical payment terms include a deposit and subsequent payments, based on specific due dates, such that all payments for the software license, data collection hardware and related ancillary products, as well as services included in the original arrangement are ordinarily due within one year of contract signing. The Company's payment terms for its indirect channel customers are less than 90 days and typically due within 30 days of invoice date.

If the payment terms for the arrangement are considered extended or if the arrangement includes a substantive acceptance provision, the Company defers revenue not meeting the criterion for recognition under SOP 97-2 and classifies this revenue as deferred revenue, including deferred product revenue. This revenue is recognized, assuming all other conditions for revenue recognition have been satisfied, when the payment of the arrangement fee becomes due and/or when the uncertainty regarding acceptance is resolved as generally evidenced by written acceptance or payment of the arrangement fee. The Company reports the allocated fair value of revenues related to the product element of arrangements as a current liability because of the expectation that these revenues will be recognized within 12 months of the balance sheet date.

Since fiscal 1996, the Company has had a standard practice of providing creditworthy end-user customers the option of financing arrangements beyond one year. These arrangements, which encompass separate fees for software license, data collection hardware and ancillary products, maintenance and support contracts and professional services, are evidenced by distinct standard sales, license and maintenance agreements and typically require equal monthly payments. The term of these arrangements typically range between 18 and 36 months. At the time the Company enters into an arrangement, the Company assesses the probability of collection and whether the arrangement fee is fixed or determinable. The Company considers its history of collection without concessions as well as whether each new transaction involves similar customers, products and arrangement economics to ensure that the history developed under previous arrangements remains relevant to current arrangements. If the fee is not determined to be collectible, fixed or determinable, the Company will initially defer the revenue and recognize when collection becomes probable, which typically is when payment is due assuming all other conditions for revenue recognition have been satisfied.

Allowance for Doubtful Accounts and Sales Returns Allowance - Kronos maintains an allowance for doubtful accounts to reflect estimated losses resulting from the inability of customers to make required payments. This allowance is based on estimates made by Kronos after consideration of factors such as the composition of the accounts receivable aging and bad debt history. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances and bad debt expense may be required. In addition, Kronos maintains a sales returns allowance to reflect estimated losses for sales returns and adjustments. Sales returns and adjustments are generally due to incorrect ordering of product, general customer satisfaction issues or incorrect billing. This allowance is established by Kronos using estimates based on historical experience. If Kronos experiences an

## Edgar Filing: KRONOS INC - Form 10-Q

increase in sales returns and adjustments, additional allowances and charges against revenue may be required.

**Valuation of Intangible Assets and Goodwill** - In assessing the recoverability of goodwill and other intangible assets, Kronos must make assumptions regarding the estimated future cash flows and other factors to determine the fair value of these assets. If these estimates or their related assumptions change in the future, Kronos may be required to record impairment charges against these assets in the reporting period in which the impairment is determined. For intangible assets, this evaluation includes an analysis of estimated future undiscounted net cash flows expected to be generated by the assets over their estimated useful lives. If the estimated future undiscounted net cash flows are insufficient to recover the carrying value of the assets over their estimated useful lives, Kronos will record an impairment charge in the amount by which the carrying value of the assets exceeds their fair value. For goodwill, the impairment evaluation includes a comparison of the carrying value of the reporting unit which houses goodwill to that reporting unit's fair value. Kronos has only one reporting unit. The fair value of the reporting unit is based upon the net present value of future cash flows, including a terminal value calculation. If the reporting unit's estimated fair value exceeds the reporting unit's carrying value, no impairment of goodwill exists. If the fair value of the reporting unit does not exceed its carrying value, then further analysis would be required to determine the amount of the impairment, if any. If Kronos determines that there is an impairment in either an intangible asset, or goodwill, Kronos may be required to record an impairment charge in the reporting period in which the impairment is determined, which may have a negative impact on earnings.

**Capitalization of Software Development Costs** - Costs incurred in the research, design and development of software for sale to others are charged to expense until technological feasibility is established. Thereafter, software development costs are capitalized and amortized to product cost of sales on a straight-line basis over the lesser of three years or the estimated economic lives of the respective products, beginning when the products are offered for sale. Costs incurred in the development of software for internal use are charged to expense until it becomes probable that future economic benefits will be realized. Thereafter, certain costs are capitalized and amortized to operating expense on a straight-line basis over the lesser of three years or the estimated economic life of the software.

### Results of Operations

**Revenues.** Revenues for the three and nine month periods ended June 28, 2003 of fiscal 2003 were \$98.2 million and \$284.4 million, respectively, as compared to \$87.1 million and \$243.1 million for the comparable periods in the prior fiscal year. Revenue growth was 13% and 17% for the three and nine month periods ended June 28, 2003, as compared to 15% and 17% for the three and nine months in the comparable periods in the prior fiscal year, respectively. Revenues from core business (business generated from customers that have not been part of an acquired business transaction over the last four fiscal quarters) accounted for 11% of the Company's revenue growth in the three month period ended June 28, 2003 and did not contribute to revenue growth in the three month period ended June 29, 2002. For the nine months ended June 28, 2003, core business growth accounted for 13% of the Company's revenue growth as compared to 5% for the comparable period in the prior fiscal year. Revenue growth attributable to acquisitions of businesses over the last four fiscal quarters was 2% and 4% for the three and nine months ended June 28, 2003, respectively, as compared to 15% and 11% for the comparable periods in the prior fiscal year.

## Edgar Filing: KRONOS INC - Form 10-Q

Product revenues for the three month period ended June 28, 2003 increased 4% to \$42.2 million as compared to \$40.5 million and a product revenue increase of 2% in the comparable period of fiscal 2002. Product revenue for the nine month period ended June 28, 2003 increased 14% to \$125.2 million as compared to \$109.7 million and a product revenue increase of 3% in the comparable period of fiscal 2002. The principal factors driving product revenue growth were increased customer demand for the newest badge terminal (Kronos' data collection device) in the three month period ended June 28, 2003, and increased customer demand for the newest badge terminal, as well as software capacity upgrades, in the nine month period ended June 28, 2003. Another factor driving product revenue growth experienced in the nine month period ended June 28, 2003 was revenues related to the conversion to Kronos products by, and add-on sales to, customers acquired from other providers of labor management solutions. Product revenue derived from acquired customers was not material in the three month period ended June 28, 2003, and \$2.4 million or 2% of total product revenue in the nine month period ended June 28, 2003. Although product revenues increased during the quarter as compared to the same period in the prior year, management believes that the continued economic environment may result in customers deferring or reducing their technology purchases in the future. While management believes the impact on technology purchasing may be temporary, the effect may cause delays or reductions in customer purchases of Kronos products and services in the future.

Maintenance revenues for the three month period ended June 28, 2003 increased 21% to \$32.8 million as compared to \$27.1 million and a maintenance revenue increase of 35% in the comparable period of fiscal 2002. Maintenance revenues for the first nine months of fiscal 2003 increased 18% to \$91.5 million as compared to \$77.5 million and a maintenance revenue increase of 33% in the first nine months of fiscal 2002. Maintenance revenue from core business accounted for 16% of Kronos' maintenance revenue growth in the three month period ended June 28, 2003 and accounted for 15% of Kronos' maintenance revenue growth in the same period of the prior fiscal year. Maintenance revenue from core business accounted for 13% of Kronos' maintenance revenue growth in the nine month period ended June 28, 2003 and accounted for 15% of Kronos' maintenance revenue growth in the same period of the prior fiscal year. Maintenance revenue growth attributable to acquisitions of businesses over the last four quarters was 5% for both the three and nine months ended June 28, 2003, as compared to 20% and 18% for the comparable periods in the prior fiscal year. The increase in core business maintenance revenues in both the three and nine month periods ended June 28, 2003 was the result of expansion of the installed base, an increase in the value of maintenance contracts, an improvement in the maintenance billing process, and incremental maintenance revenues attributable to customers obtained from the acquisition of businesses. The increase in the value of the maintenance contracts was principally attributable to the platform upgrade of existing customers to Kronos' new products. Platform and capacity upgrade sales typically result in an increased value of maintenance contracts.

Professional services revenues for the three month period ended June 28, 2003 increased 19% to \$23.2 million as compared to \$19.5 million and a professional services revenue increase of 22% in the comparable period of fiscal 2002. Professional service revenues for the first nine months of fiscal 2003 increased 21% to \$67.7 million as compared to an increase of 27% to \$56.0 million in the first nine months of fiscal 2002. Professional services revenue from core business accounted for 16% of Kronos' professional services revenue growth in the three month period ended June 28, 2003 and accounted for 7% of Kronos' professional services revenue growth in the same period of the prior fiscal year. Professional services revenue from core business accounted for 17% of Kronos' professional services revenue growth in the nine month period ended June 28, 2003 and accounted for 15% of Kronos' professional services revenue

## Edgar Filing: KRONOS INC - Form 10-Q

growth in the same period of the prior fiscal year. Professional services revenue growth attributable to acquisitions of businesses over the last four quarters was 3% and 4% for the three and nine months ended June 28, 2003, respectively, as compared to 15% and 12% for the comparable periods in the prior fiscal year. The growth in core business professional services revenues in both the three and nine month periods ended June 28, 2003, was primarily due to an increase in the level of professional services accompanying new and platform upgrade sales and an increase in demand for Kronos' services. The growth in professional service revenues for the three and nine months ended June 29, 2002 reflected an increase in the level of professional services accompanying new and upgrade sales, an increase in the level of follow-on services sold to the installed base, and an increase in delivery of professional services resulting from improving the efficiency of Kronos services organization.

Deferred maintenance revenues increased 8% from September 30, 2002. Current deferred maintenance revenues increased 11% and long-term deferred maintenance revenues decreased 19% from September 30, 2002. Maintenance revenues have grown at a faster rate than deferred maintenance primarily due to the positive impact on the improvement in the billing process which appropriately captures the effective date of contract reinstatements, as well as the effect of the timing of the expiration of multi-year maintenance contracts sold in previous fiscal years and the effect of acquisitions completed near the end of the previous fiscal year. The decrease in the long-term portion was due to Kronos' decision in fiscal 2000 to curtail the practice of selling multi-year maintenance contracts. Deferred professional services revenues increased 3% from September 30, 2002. Professional services revenues have grown at a faster rate than the deferred professional services primarily due to an increase in the level of professional services that are billed in arrears as services are delivered, as well as an increase in the utilization efficiency of the service organization as compared to the prior fiscal year.

Gross Profit. Gross profit as a percentage of revenues was 61% for both the three and nine month periods ended June 28, 2003, respectively, as compared to 60% in the three month period ended June 29, 2002 and 61% in the nine month period ended June 29, 2002. The increase in gross profit for the three month period ended June 28, 2003, as compared to the same period in the prior year is attributable to an increase in service gross profit and, to a lesser extent, an increase in product gross profit. Product gross profit as a percentage of product revenues was 76% for both the three and nine month periods ended June 28, 2003, respectively, compared to 75% both the three and nine month periods of the prior fiscal year. This increase in product gross profit is primarily attributable to favorable product mix and manufacturing volume. During the three month period ended June 28, 2003, the product mix contained a lower proportion of third party products for re-sale, which typically generate lower margins. In addition, an increase in the volume of badge terminals sold resulted in lower production costs per unit. Service gross profit as a percentage of service and maintenance revenues was 50% and 49% for the three and nine month periods ended June 28, 2003, respectively, as compared to 47% and 49% in the same periods of the prior fiscal year, respectively. This increase in service gross profit for the three month period ended June 28, 2003, as compared to the same period last year was primarily the result of increased productivity in the service organization. The improvement in productivity is the result of leveraging and effectively managing the resources required to deliver customer support. Management anticipates overall gross profit in the fourth quarter of fiscal 2003 to exceed that experienced in the three month period ended June 28, 2003 despite anticipating that more revenue will be derived from newer products including its Kronos 4500 terminal and HRMS products, which carry higher production and royalty costs, and increased investment in infrastructure to support the introduction of its HRMS products.

## Edgar Filing: KRONOS INC - Form 10-Q

Net Operating Expenses. Net operating expenses for the three months ended June 28, 2003 increased \$4.4 million, or 10%, to \$46.6 million as compared to an increase of \$1.2 million, or 3%, to \$42.2 million for the comparable period in the prior fiscal year. For the nine month period ended June 28, 2003, net operating expenses increased \$17.2 million, or 14%, to \$136.6 million as compared to an increase of \$2.5 million, or 2%, to \$119.4 million for the comparable period in the prior fiscal year. The increase in actual spending for the three and nine month periods ended June 28, 2003, as compared to the same periods in the prior fiscal year was primarily attributable to investments in personnel and related compensation and support costs, including those associated with the introduction of the new HRMS products, as well as increased spending for outside consultants and professional fees, training costs, and additional investment in infrastructure costs required to support higher sales volumes. As a percentage of revenues, net operating expenses were 47% for the three month period ended June 28, 2003, and 48% for the nine month period ended June 28, 2003, as compared to 49% for both the three and nine month periods ended June 29, 2002. The reduction in net operating expenses as a percentage of revenues was attributable to the leveraging of investments in infrastructure to generate higher sales volumes, and continued corporate-wide efforts to contain costs. Although management intends to decrease operating expenses as a percentage of revenues during the remainder of fiscal 2003, principally through continued productivity improvements, uncertainty related to the current economic climate and its impact on the timing of customers' purchases, as well as increased investments in productivity programs and infrastructure to support the introduction of the new HRMS products, may prevent decreases in operating expenses as a percentage of revenues from being realized.

Sales and marketing expenses increased \$2.7 million, or 10%, to \$31.1 million for the three month period ended June 28, 2003 as compared to an increase of \$2.3 million, or 9%, to \$28.3 million in the comparable period of fiscal 2002. For the first nine months of fiscal 2003, sales and marketing expenses increased \$11.9 million, or 15%, to \$91.5 million as compared to an increase of \$6.6 million, or 9%, to \$79.6 million for the first nine months of fiscal 2002. The increase in sales and marketing spending was attributable to Kronos' investments in sales personnel and related compensation and support costs to maximize the penetration of existing accounts and to add new customers, additional spending for personnel training, as well as initiatives to expand market awareness of Kronos products and services. As a percentage of revenues, sales and marketing were 32% for both three and nine month periods ended June 28, 2003, as compared to 33% for the same periods in the prior fiscal year. The decrease in sales and marketing expense as a percentage of revenues was primarily due to leveraging the investments in infrastructure to generate higher sales volumes.

Engineering, research and development expenses have increased \$0.9 million, or 10%, to \$9.9 million for the quarter as compared to a decrease of \$0.1 million, or 1%, to \$9.0 million for the same period in the prior fiscal year. For the nine months ended June 28, 2003 engineering, research and development expenses increased \$1.7 million, or 7%, to \$27.9 million as compared to an increase of \$0.8 million, or 3%, to \$26.2 million for the first nine months of fiscal 2002. The increase in spending in the three month period ended June 28, 2003, as compared to the same period in the prior fiscal year, was primarily due to an increase in compensation related expenses, including those associated with the introduction of the new HRMS products, and an increase in costs associated with engineering consultants, partially offset by the reallocation of certain engineering resources focused upon information systems support to general and administrative expenses. The increase in spending in the first nine months of fiscal 2003, as compared to the same period in the prior fiscal year, was principally due to an increase in compensation related expenses, as well as an increase in training expenses and an increase in costs associated with

## Edgar Filing: KRONOS INC - Form 10-Q

engineering consultants, partially offset by the previously discussed reallocation of engineering resources to general and administrative expenses. Engineering, research and development expenses as a percentage of revenues were 10% for both the three and nine month periods ended June 28, 2003, as compared to 10% and 11% for the same periods in the prior fiscal year. The decrease as a percentage of revenues for the nine months ended June 28, 2003, as compared to the same period in the prior fiscal year, was primarily due to higher sales volume in fiscal 2003. Engineering, research and development expenses of \$9.9 million and \$9.0 million in the third quarter of fiscal 2003 and 2002, respectively, are net of capitalized software development costs of \$3.1 million and \$3.0 million, respectively, for each quarter. Engineering, research and development expenses of \$27.9 million and \$26.2 million in the first nine months of fiscal 2003 and 2002, respectively, are net of capitalized software development costs of \$9.0 million and \$8.4 million, respectively. The significant project development efforts in the first nine months of fiscal 2003 principally related to further development and enhancement of the Workforce Central(R) suite, Workforce HR(TM), Workforce Payroll(TM), Kronos 4500(TM) terminal and, to a lesser extent, the eForce(R) software acquired from SimplexGrinnell on December 28, 2001.

General and administrative expenses increased \$0.6 million, or 10%, to \$6.1 million for the three month period ended June 28, 2003 as compared to an increase of \$0.6 million, or 11%, to \$5.5 million in the comparable period of fiscal 2002. For the first nine months of 2003, general and administrative expenses increased \$3.4 million, or 22%, to \$18.5 million as compared to an increase of \$1.5 million, or 11%, to \$15.1 million for the first nine months of fiscal 2002. The increase in general and administrative expenses in the three and nine month periods ended June 28, 2003 was primarily due to Kronos' investment in personnel and related compensation and support costs (including those costs associated with the previously discussed reallocation of engineering resources to general and administrative expenses), an increase in fees related to tax planning services, an increase in bad debt expense and continued investment in other infrastructure to support the growth of operations. General and administrative expenses as a percentage of revenues were 6% and 7% for the three and nine month periods ended June 28, 2003, respectively, as compared to 6% for the same periods in the prior fiscal year. General and administrative expenses primarily consist of personnel and overhead related expenses for administrative, information technology, finance, legal and human resources support functions.

Amortization of intangible assets as a percentage of revenues were 1% for all periods presented. Other income, net as a percentage of revenues were 1% in both the three and nine month periods ended June 28, 2003, as compared to 2% for the same periods in the prior fiscal year. Other income, net is principally interest income earned from Kronos' cash as well as investments in its marketable securities and financing arrangements.

Income Taxes. The provision for income taxes as a percentage of pretax income was 37.2% in the three month period ended June 28, 2003, and 36.5% for the nine month period ended June 28, 2003. As a percentage of pretax income, the three month period ended June 29, 2002 had a tax provision of 34.8% and the nine month period ended June 29, 2002 had a tax provision of 34.8%. Kronos' effective income tax rate may fluctuate between periods as a result of various factors, including income tax credits, foreign tax rate differentials and state income taxes.

Newly Issued Accounting Standards. In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123." This statement provides alternative methods of transition for a voluntary change to the fair value method of



## Edgar Filing: KRONOS INC - Form 10-Q

accounting for stock-based compensation. The statement amends the disclosure requirements of FASB Statement No. 123 to require prominent disclosure in both annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. Kronos accounts for stock-based compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and complies with the disclosure provisions of FASB Statement No. 123. The transition provisions are effective for fiscal years ending after December 15, 2002. The disclosure provisions are effective for interim periods beginning after December 15, 2002. Kronos implemented the required disclosure provisions in the three month period ended March 29, 2003. The adoption of this statement is not expected to have a material impact on Kronos' consolidated financial position, results of operations or cash flows as Kronos does not anticipate making the voluntary change to the fair value method of accounting for stock-based compensation.

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities, an interpretation of Accounting Research Bulletin No. 51." FIN No. 46 requires certain variable interest entities, or VIEs, to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN No. 46 is effective for all VIEs created or acquired after January 31, 2003. For VIEs created or acquired prior to February 1, 2003, the provisions of FIN No. 46 must be applied for the first interim or annual period beginning after June 15, 2003. Kronos currently has no contractual relationship or other business relationship with a variable interest entity and therefore the adoption of FIN No. 46 did not have a material effect on Kronos' consolidated financial position, results of operations or cash flows. However, if Kronos enters into any such arrangement with a VIE in the future, Kronos' consolidated financial position or results of operations may be adversely affected.

### Liquidity and Capital Resources

Kronos funds its business through cash generated by operations. If near-term demand for Kronos' products weakens or if significant anticipated sales in any quarter do not close when expected, the availability of such funds may be adversely impacted. If the need arose, Kronos believes that based on its current debt-free balance sheet and its financial position, it would be successful in securing financing from the capital markets.

Cash, cash equivalents and marketable securities (which includes both short and long term securities) amounted to \$103.1 million as of June 28, 2003, and \$74.7 million as of September 30, 2002. This increase in cash, cash equivalents and marketable securities is due to cash generated from operations. Working capital as of June 28, 2003 amounted to \$9.3 million as compared with \$2.4 million at September 30, 2002. This increase in working capital is primarily due to an increase in cash resulting from cash provided by operations.

Cash provided by operations amounted to \$53.2 million in the first nine months of fiscal 2003 as compared to \$42.7 million in the first nine months of fiscal 2002. The increase in operating cash flows in fiscal 2003 is principally attributable to higher net income, increased non-cash charges that are added back in the calculation of cash flow from operations, as well as the net positive impact of changes in accounts receivable, deferred revenues, accounts payable and accrued expenses. In addition, although the tax benefit from exercise of stock options contributed less to cash flow from operations in the first nine months of fiscal 2003, as compared to the same period last fiscal year, the related increase in taxes payable more than offsets this effect.

Edgar Filing: KRONOS INC - Form 10-Q

Cash used for property, plant and equipment was \$8.5 million in the first nine months of fiscal 2003 compared to \$8.3 million in the first nine months of fiscal 2002. Kronos' use of cash for property, plant and equipment in both periods presented includes investments in information system and infrastructure to improve and support expanding operations. Kronos' use of cash for the acquisition of businesses and software for the nine months ended June 28, 2003 and June 29, 2002 was principally related to the acquisitions of specified assets and/or businesses of Kronos' dealers and/or other providers of labor management solutions. In addition, during the first nine months of fiscal 2002, Kronos' use of cash for the acquisition of businesses and software included cash used for the acquisition of the source code license for the Abra Enterprise human resources and payroll software. Kronos is assessing several acquisition opportunities that may be completed over the next twelve months, although there can be no assurance that these acquisitions will be completed. Excess cash reserves not required for operations, investments in property, plant and equipment or acquisitions are invested in marketable securities. Net investments in marketable securities increased by \$17.9 million in the first nine months of fiscal 2003 compared to an increase of \$3.5 million in the first nine months of fiscal 2002.

Under Kronos' stock repurchase program, Kronos repurchased 356,700 common shares in the first nine months of fiscal 2003 at a cost of \$13.2 million, compared to 396,950 common shares at a cost of \$17.0 million for the same period in the prior fiscal year. The common shares repurchased under the program are used for Kronos' employee stock option plans and employee stock purchase plan. During the first quarter of fiscal 2003, Kronos received \$2.6 million upon the maturity of a call option arrangement. As of June 28, 2003, Kronos did not have any outstanding call option arrangements. Please refer to Note I in the Notes to Condensed Consolidated Financial Statements for further details regarding call option arrangements. Cash provided by operations was sufficient to fund investments in capitalized software development costs, property, plant and equipment and stock repurchases.

Kronos leases certain office space, manufacturing facilities and equipment under long-term operating lease agreements. In addition, certain acquisition agreements contain provisions that require Kronos to make a guaranteed payment and/or contingent payments based upon profitability of the business unit or if specified minimum revenue requirements are met. Future minimum rental commitments under operating leases with noncancellable terms of one year or more, and future payment obligations related to guaranteed payments are as follows (in thousands):

Contractual Obligations	Payments Due by Period				More than 5 years
	Total	Less than 1 year	1-3 years	3-5 years	
Operating Lease Obligations	\$35,847	\$ 9,619	\$15,749	\$ 7,752	\$
Guaranteed Payment Obligations .....	5,071	2,959	2,000	112	
Total .....	\$40,918	\$12,578	\$17,749	\$ 7,864	\$

## Edgar Filing: KRONOS INC - Form 10-Q

Kronos believes that with cash generated from ongoing operations it has adequate cash and investments and operating cash flow to fund its investments in property, plant and equipment, software development costs, cash requirements under operating leases, cash payments related to acquisitions, if any, and any additional stock repurchases for the foreseeable future.

During the three months ended June 28, 2003, Kronos did not engage in:

- o material off-balance sheet activities, including the use of structured finance or special purpose entities,
- o material trading activities in non-exchange traded commodity contracts, or
- o transactions with persons or entities that benefit from their non-independent relationship with Kronos.

### Certain Factors That May Affect Future Operating Results

Except for historical matters, the matters discussed in this Quarterly Report on Form 10-Q are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 (the "Act"). Kronos desires to take advantage of the safe harbor provisions of the Act and is including this statement for the express purpose of availing itself of the protection of the safe harbor with respect to all forward-looking statements that involve risks and uncertainties.

Kronos' actual operating results may differ from those indicated by forward-looking statements made in this Quarterly Report on Form 10-Q and presented elsewhere by management from time to time because of a number of factors including the potential fluctuations in quarterly results, timing and acceptance of new product introductions by Kronos and its competitors, the dependence on Kronos' time and attendance product line, the ability to attract and retain sufficient technical personnel, the protection of Kronos' intellectual property and the potential infringement on Kronos' intellectual property rights, competitive pricing pressure, and the dependence on alternate distribution channels and on key vendors, as further described below and in Kronos' Annual Report on Form 10-K for the fiscal year ended September 30, 2002, which are specifically incorporated by reference herein.

**Potential Fluctuations in Results.** Kronos' operating results, including revenue growth, sources of revenue, effective tax rate and liquidity, may fluctuate as a result of a variety of factors, including the purchasing patterns of its customers, mix of products and services sold, the ability of Kronos to effectively integrate acquired businesses into Kronos' operations, the timing of the introduction of new products and product enhancements by Kronos and its competitors, the strategy employed by Kronos to enter the Human Resources Management System ("HRMS") market, market acceptance of new products, competitive pricing pressure and general economic conditions. Kronos historically has realized a relatively larger percentage of its annual revenues and profits in the third and fourth quarters and a relatively smaller percentage in the first and second quarters of each fiscal year, although there can be no assurance that this pattern will continue. In addition, substantially all of Kronos' product revenue and profits in each quarter result from orders received in that quarter. If near-term demand for Kronos' products weakens or if significant anticipated sales in any quarter do not close when expected, Kronos' revenues for that quarter will be adversely affected. Kronos believes that its

## Edgar Filing: KRONOS INC - Form 10-Q

operating results for any one period are not necessarily indicative of results for any future period.

**Dependence on Labor Management Product Line.** To date, more than 90% of Kronos' revenues have been attributable to sales of labor management systems and related services. Although Kronos has introduced its products for the licensed HRMS market during fiscal 2002, Kronos expects that its dependence on the labor management product line for revenues will continue for the foreseeable future. Competitive pressures or other factors could cause Kronos' labor management products to lose market acceptance or experience significant price erosion, adversely affecting the results of Kronos' operations.

**Product Development and Technological Change.** Continual change and improvement in computer software and hardware technology characterize the markets for labor management systems. Kronos' future success will depend largely on its ability to enhance the capabilities and increase the performance of its existing products and to develop new products and interfaces to third-party products on a timely basis to meet the increasingly sophisticated needs of its customers. Although Kronos is continually seeking to further enhance its labor management, HR and payroll product offerings (including products for the HRMS market) and to develop new products and interfaces, there can be no assurance that these efforts will succeed, or that, if successful, such product enhancements or new products will achieve widespread market acceptance, or that Kronos' competitors will not develop and market products which are superior to Kronos' products or achieve greater market acceptance.

**Dependence on Alternate Distribution Channels.** Kronos markets and sells its products through its direct sales organization, independent resellers and ADP under an OEM agreement. In the first nine months of fiscal 2003, approximately 9% of Kronos' revenue was generated through sales to resellers and ADP. Management does not anticipate that its entrance into the HRMS market will have a negative impact on its relationship with ADP. However, a reduction in the sales efforts of either Kronos' major resellers or ADP, or termination or changes in their relationships with Kronos, could have a material adverse effect on the results of Kronos' operations. Earlier in fiscal 2003, Kronos and ADP signed a letter of intent to extend their business relationship for an additional term of five years.

**Competition.** The labor management industry is highly competitive. Technological changes such as those allowing for increased use of the Internet have resulted in new entrants into the market. Although Kronos believes it has core competencies that position it strongly in the marketplace, maintaining Kronos' technological and other advantages over competitors will require continued investment by Kronos in research and development and marketing and sales programs. There can be no assurance that Kronos will have sufficient resources to make such investments or be able to achieve the technological advances necessary to maintain its competitive advantages. Increased competition could adversely affect Kronos' operating results through price reductions and/or loss of market share. With Kronos' efforts to expand its labor management offering with the recent introduction of its HRMS product suite, Kronos will continue to meet strong competition. Many of these competitors may be able to adapt more quickly to new or emerging technologies or to devote greater resources to the promotion and sale of their HRMS products. Many of Kronos' HRMS competitors have significantly greater financial, technical and sales and marketing resources than Kronos, as well as more experience in delivering HRMS solutions. There can be no assurance that Kronos will be able to compete successfully in the HRMS marketplace, and its failure to do so could have a material adverse impact upon its business, prospects, financial condition and operating results.

## Edgar Filing: KRONOS INC - Form 10-Q

Attracting and Retaining Sufficient Technical Personnel for Product Development, Support and Sales. Kronos has encountered intense competition for experienced technical personnel for product development, technical support and sales and expects such competition to continue in the future. Any inability to attract and retain a sufficient number of qualified technical personnel could adversely affect Kronos' ability to produce, support and sell products in a timely manner.

Protection of Intellectual Property. Kronos has developed, and through its acquisitions of businesses and software, acquired proprietary technology and intellectual property rights. Kronos' success is dependent upon its ability to further develop and protect its proprietary technology and intellectual property rights. Kronos seeks to protect products, software, documentation and other written materials primarily through a combination of trade secret, patent, trademark and copyright laws, confidentiality procedures and contractual provisions. While Kronos has attempted to safeguard and maintain its proprietary rights, it is unknown whether Kronos has been or will be successful in doing so.

Despite Kronos' efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of its products or obtain and use information that is regarded as proprietary. Policing unauthorized use of Kronos' products is difficult. While Kronos is unable to determine the extent to which piracy of its software products exists, software piracy can be expected to be a persistent problem, particularly in foreign countries where the laws may not protect proprietary rights as fully as in the United States. Kronos can offer no assurance that it can adequately protect its proprietary rights or that its competitors will not reverse engineer or independently develop similar technology.

Infringement of Intellectual Property Rights. Kronos cannot provide assurance that others will not claim that Kronos developed or acquired intellectual property rights infringe on their intellectual property rights or that Kronos does not in fact infringe on those intellectual property rights.

Any litigation regarding intellectual property rights could be costly and time-consuming and divert the attention of Kronos' management and key personnel from business operations. The complexity of the technology involved and the uncertainty of intellectual property litigation increase these risks. Claims of intellectual property infringement might also require Kronos to enter into costly royalty or license agreements, and in this event, Kronos may not be able to obtain royalty or license agreements on acceptable terms, if at all. Kronos may also be subject to significant damages or an injunction against the use of its products. A successful claim of patent or other intellectual property infringement against Kronos could cause immediate and substantial damage to its business and financial condition.

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

Kronos is exposed to a variety of market risks, including changes in interest rates affecting the return on its investments, foreign currency fluctuations and decreases in its common stock price affecting capped call options. Refer to Note A "Summary of Significant Accounting Policies" in the Notes to Consolidated Financial Statements in the Annual Report on Form 10-K for the year ended September 30, 2002 for further discussion regarding marketable securities, foreign currency forward exchange contracts and capped call option arrangements. Kronos' marketable securities that expose it to market rate risks are comprised of debt securities. A decrease in interest rates would not adversely impact interest income or related cash flows pertaining to securities held at June 28, 2003, as all of these securities have fixed rates of interest. A 100 basis point increase in interest rates would not adversely impact the fair

## Edgar Filing: KRONOS INC - Form 10-Q

value of these securities by a material amount due to the size and average duration of the portfolio. Kronos' exposure to market risk for fluctuations in foreign currency relate primarily to the amounts due from subsidiaries. Exchange gains and losses related to amounts due from subsidiaries have not been material. For foreign currency exposures existing at June 28, 2003, a 10% unfavorable movement in the foreign exchange rates for each subsidiary location would not expose the Company to material losses in earnings or cash flows. The calculation assumes that each exchange rate would change in the same direction relative to the U.S. dollar.

Kronos has periodically entered into short term capped call options in conjunction with its stock repurchase initiatives. As of June 28, 2003, there were no capped call option arrangements outstanding.

### Item 4. Controls and Procedures.

#### (a) Evaluation of Disclosure Controls and Procedures

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of June 28, 2003. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that, as of June 28, 2003, the Company's disclosure controls and procedures were (1) designed to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to the Company's Chief Executive Officer and Chief Financial Officer by others within those entities, particularly during the period in which this report was being prepared and (2) effective, in that they provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

#### (b) Changes in Internal Controls

No change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended June 28, 2003 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 6. Exhibits and Reports on Form 8-K

#### (a) Exhibits

- 31.1 Certification by Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
- 31.2 Certification by Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
- 32.1 Certificate by Chief Executive Officer and Chief Financial

Edgar Filing: KRONOS INC - Form 10-Q

Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

10.1(1) Kronos Incorporated 2003 Employee Stock Purchase Plan as amended.

(b) Reports on Form 8-K

On July 24, 2003, the Company furnished a Current Report on Form 8-K under Item 9, containing a copy of its earnings release, dated July 24, 2003, for the period ending June 28, 2003 pursuant to Item 12 (Results of Operations and Financial Condition).

(1) Incorporated by Reference to the Registrants Form S-8 filed on August 1, 2003 (File No. 333-107572)

SIGNATURES

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

KRONOS INCORPORATED

August 8, 2003

By /s/ Paul A. Lacy

-----  
Paul A. Lacy  
Executive Vice President,  
Chief Financial and Administrative Officer  
(Duly Authorized Officer and  
Principal Financial Officer)

KRONOS INCORPORATED

EXHIBIT INDEX

Exhibit Number	Description
-----	-----
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification by Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certificate by Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
10.1(1)	Kronos Incorporated 2003 Employee Stock Purchase Plan as amended.

## Edgar Filing: KRONOS INC - Form 10-Q

- (1) Incorporated by Reference to the Registrant's Form S-8 filed on August 1, 2003 (File No. 333-107572).

Exhibit 31.1

### CERTIFICATIONS

I, Mark S. Ain, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Kronos Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) [Paragraph omitted in accordance with SEC transition instructions contained in SEC Release 34-47986]
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to



## Edgar Filing: KRONOS INC - Form 10-Q

record, process, summarize and report financial information; and

- b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 8, 2003

/s/ Mark S. Ain

-----  
Mark S. Ain  
Chief Executive Officer

Exhibit 31.2

### CERTIFICATIONS

I, Paul A. Lacy, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Kronos Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) [Paragraph omitted in accordance with SEC transition instructions contained in SEC Release 34-47986]
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on

Edgar Filing: KRONOS INC - Form 10-Q

our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

- a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 8, 2003

/s/ Paul A. Lacy

-----  
Paul A. Lacy  
Executive Vice President, Chief Financial  
and Administrative Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Kronos Incorporated (the "Company") for the period ended June 28, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Mark S. Ain, Chief Executive Officer of the Company, and Paul A. Lacy, Executive Vice President, Chief Financial and Administrative Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Mark S. Ain

Dated: August 8, 2003

-----  
Mark S. Ain  
Chief Executive Officer

/s/ Paul A. Lacy

Dated: August 8, 2003

-----  
Paul A. Lacy  
Executive Vice President, Chief Financial  
and Administrative Officer

A signed original of this written statement required by Section 906 has been

Edgar Filing: KRONOS INC - Form 10-Q

provided to Kronos Incorporated and will be retained by Kronos Incorporated and furnished to the Securities and Exchange Commission or its staff upon request.