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KRONOS INC
Form 10-Q
August 10, 2001

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 30, 2001

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

As of July 28, 2001, 12,579,925 shares of the registrant's Common Stock,
\$.01 par value, were outstanding.

KRONOS INCORPORATED

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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	
	June 30, 2001	July 1, 2000
	-----	-----
Net revenues:		
Product	\$ 39,524	\$ 38,602
Service	35,596	29,531
	-----	-----
	75,120	68,133
Cost of sales:		
Product	8,311	8,729
Service	19,194	17,813
	-----	-----
	27,505	26,542
	-----	-----
Gross profit	47,615	41,591

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Operating expenses and other income:		
Sales and marketing	25,974	24,147
Engineering, research and development	9,107	7,245
General and administrative	4,954	4,409
Amortization of intangible assets	1,860	1,704
Other income, net	(1,621)	(1,171)
Special charge	698	--
	-----	-----
	40,972	36,334
Income before income taxes	6,643	5,257
Income tax provision	2,325	1,945
	-----	-----
Net income	\$ 4,318	\$ 3,312
	=====	=====
Net income per common share:		
Basic	\$ 0.35	\$ 0.27
	=====	=====
Diluted	\$ 0.34	\$ 0.26
	=====	=====
Average common and common equivalent shares outstanding:		
Basic	12,500,012	12,404,310
	=====	=====
Diluted	12,776,520	12,734,592
	=====	=====

See accompanying notes to condensed consolidated financial statements.

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

	June 30, 2001	S
	-----	-----
ASSETS		
Current assets:		
Cash and equivalents	\$ 20,470	
Marketable securities	31,310	
Accounts receivable, less allowances of \$7,305 at June 30, 2001 and \$6,986 at September 30, 2000	59,336	
Deferred income taxes	5,991	
Other current assets	17,373	

Total current assets	134,480	
Property, plant and equipment, net	35,805	
Marketable securities	16,400	
Excess of cost over net assets of businesses acquired, net	29,589	
Deferred software development costs, net	16,023	
Other assets	13,732	

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Total assets	\$ 246,029
	=====
LIABILITIES AND SHAREHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	\$ 6,786
Accrued compensation	20,321
Accrued expenses and other current liabilities	10,914
Deferred professional service revenues	24,979
Deferred maintenance revenues	51,906

Total current liabilities	114,906
Deferred maintenance revenues	12,145
Other liabilities	1,747
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 20,000,000 shares, 12,634,728 shares issued at June 30, 2001 and September 30, 2000	126
Additional paid-in capital	17,290
Retained earnings	104,018
Accumulated other comprehensive loss	(1,385)
Cost of Treasury Stock (78,129 shares and 310,038 shares at June 30, 2001 and September 30, 2000, respectively)	(2,818)

Total shareholders' equity	117,231

Total liabilities and shareholders' equity	\$ 246,029
	=====

See accompanying notes to condensed consolidated financial statements.

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

	Nine

	June 30,
	2001

Operating activities:	
Net income	\$ 6,174
Adjustments to reconcile net income to net cash and equivalents provided by operating activities:	
Depreciation	5,986
Amortization of excess of cost over net assets of businesses acquired	5,447
Amortization of deferred software development costs	6,257
Provision for deferred income taxes	1,171
Changes in certain operating assets and liabilities:	
Accounts receivable, net	11,979
Deferred maintenance revenue	(1,978)
Accounts payable, accrued compensation and other liabilities	(3,452)

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Long term investment in leases	2,072
Non cash portion of special charge	1,300
Other	(3,162)
Tax benefit from exercise of stock options	2,528

Net cash and equivalents provided by operating activities	34,322
 Investing activities:	
Purchase of property, plant and equipment	(4,606)
Capitalization of software development costs	(9,003)
(Increase) decrease in marketable securities	(19,470)
Acquisitions of businesses, net of cash acquired	(4,311)

Net cash and equivalents used in investing activities	(37,390)
 Financing activities:	
Net proceeds from exercise of stock option and employee stock purchase plans	8,357
Purchase of treasury stock	(7,833)
Proceeds from sale of put options	--

Net cash and equivalents used in financing activities	524
Effect of exchange rate changes on cash and equivalents	(187)

Decrease in cash and equivalents	(2,731)
Cash and equivalents at the beginning of the period	23,201

Cash and equivalents at the end of the period	\$ 20,470
	=====

See accompanying notes to condensed consolidated financial statements.

KRONOS INCORPORATED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A - General

The accompanying unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring accruals that management of Kronos Incorporated (the "Company") 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, 2000. The results of operations for the three and nine months ended June 30, 2001 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 2001 presentation.

Note B - Newly Issued Accounting Standards

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In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, "Business Combinations", and No. 142, "Goodwill and Other Intangible Assets", effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill (and intangible assets deemed to have indefinite lives) will no longer be amortized but will be subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives.

For acquisitions completed prior to June 30, 2001, the Company will apply the new rules on accounting for business combinations and goodwill and other intangible assets beginning in the first quarter of fiscal year 2002. For acquisitions completed after June 30, 2001, the Company will apply the new rules beginning in the fourth quarter of fiscal year 2001. The Company has not yet determined the effect that the application of the non-amortization provisions of the Statements will have on net income. During fiscal year 2002, the Company will perform the first of the required impairment tests of goodwill as of October 1, 2001 and has not yet determined what the effect of these tests will be on earnings and financial position of the Company.

NOTE C - 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 (91 days in fiscal 2001 and 93 days in fiscal 2000) and fourth quarter (92 days in fiscal 2001 and 91 days in fiscal 2000) 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 D - Special Charge

A special charge in the amount of \$700,000 was recorded in this quarter related to termination costs from a reduction in workforce of approximately 90 employees. At June 30, 2001, the outstanding liability related to this charge was approximately \$100,000, which is anticipated to be paid within the next three months.

During the second quarter of 2001, the Company commenced the shut down of its Crosswinds Technology Group operations located in Santa Cruz, California, which resulted in a \$3.0 million charge to operating income in that quarter. The charge included \$1.6 million in termination costs, \$1.3 million for the write off of intangible assets, and \$100,000 in other costs. Approximately 19 employees were affected by this action. Of the \$1.7 million liability recorded in March 2001, \$1.2 million remains outstanding as of June 30, 2001. The Company expects to settle these liabilities within the next nine months.

The components of the liabilities related to the second and third quarter special charges are listed below.

Accrual for special charges (in thousands):

Description	Balance at March 31,	Additional Charges	Cash Outlays	Balance at June 30,
-------------	-------------------------	-----------------------	-----------------	------------------------

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	2001		2001	
	-----	-----	-----	-----
Termination costs	\$ 1,600	\$ 700	\$ (1,100)	\$ 1,200
Other costs	100	--	--	100
Total accrual ...	<u>\$ 1,700</u>	<u>\$ 700</u>	<u>\$ (1,100)</u>	<u>\$ 1,300</u>

NOTE E - Comprehensive Income

For the three and nine months ended June 30, 2001 and July 1, 2000 comprehensive income consisted of the following (in thousands):

	Three Months Ended		Nine Months Ended	
	June 30, 2001	July 1, 2000	June 30, 2001	July 1, 2000
	-----	-----	-----	-----
Comprehensive income:				
Net income	\$ 4,318	\$ 3,312	\$ 6,174	\$ 9,517
Cumulative translation adjustment	216	(236)	(325)	(545)
Unrealized (loss)gain				
on	(100)	(206)	306	(206)
available-for-sale securities				
Total comprehensive income	<u>\$ 4,434</u>	<u>\$ 2,870</u>	<u>\$ 6,155</u>	<u>\$ 8,766</u>

NOTE F - Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended		Nine Months Ended	
	June 30, 2001	July 1, 2000	June 30, 2001	July 1, 2000
	-----	-----	-----	-----
Net income (in thousands)	<u>\$ 4,318</u>	<u>\$ 3,312</u>	<u>\$ 6,174</u>	<u>\$ 9,517</u>
Weighted-average shares	12,500,012	12,404,310	12,455,724	12,460,000
Effect of dilutive securities:				
Put options	--	--	--	10,000
Employee stock options	276,508	330,282	360,777	545,000

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Adjusted weighted-average shares and assumed conversions	12,776,520 =====	12,734,592 =====	12,816,501 =====	13,016, =====
Basic earnings per share	\$ 0.35 =====	\$ 0.27 =====	\$ 0.50 =====	\$ 0 =====
Diluted earnings per share	\$ 0.34 =====	\$ 0.26 =====	\$ 0.48 =====	\$ 0 =====

G. Subsequent Event

On July 1, 2001, the Company acquired substantially all of the assets of a competing provider of labor management solutions to the U.S. healthcare industry. Cash held in escrow at June 30, 2001, pending the completion of this acquisition, amounted to \$10.5 million and included \$1.5 million for the prepayment of certain account receivable balances. This acquisition will be accounted using the purchase method of accounting and will not materially impact the Company's results of operations or financial condition. As a result, no pro forma information has been presented.

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 demand for products and services, revenue growth rates and gross margin, management of dealer channels, future acquisitions and available cash, investments and operating cash flow. 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" at the end of Management's Discussion and Analysis of Financial Condition and Results of Operations.

Results of Operations

Revenues. Revenues for the three and nine months ended June 30, 2001 were \$75.1 million and \$206.9 million, respectively, as compared to \$68.1 million and \$194.6 million for the comparable periods in the prior year. Revenue growth in the three and nine months ended June 30, 2001 were 10% and 6%, respectively, as compared to 1% and 7% growth in the comparable periods of the prior year. The revenue growth rate experienced in the third quarter of fiscal 2001 compares favorably to the comparable quarter of the prior year principally due to the unusually low growth rate experienced in the third quarter of fiscal 2000. Although the revenue growth rate experienced in the first nine months of fiscal 2001 is comparable to the growth rate experienced in the same period of the prior year, the revenue growth rate experienced from the second quarter of fiscal 2000 through the first quarter of fiscal 2001 was nominal due principally to the transitory impact on demand for Kronos' products and services as a result of Year 2000 compliance efforts and the broad economic downturn. The revenue growth rates experienced in the second and third quarters of fiscal 2001 have improved in comparison to the preceding four quarters, principally due to demand

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for Kronos' services. Management believes that demand for Kronos' products and services continues to exist. Although, the revenue growth rate in the fourth quarter is anticipated to be positive, uncertainty exists given the broad economic downturn and the possibility of companies postponing technology spending.

Product revenues for the quarter increased 2% to \$39.5 million as compared to \$38.6 million and a product revenue decline of 12% in the third quarter of fiscal 2000. Product revenues for the first nine months of fiscal 2001 declined 1% to \$105.6 million compared to \$106.8 million and a product revenue decline of 9% in the first nine months of fiscal 2000. The product revenue growth experienced in the third quarter was principally the result of customer demand in Kronos' direct sales channel. Product revenues from Kronos' independent dealer channel in the third quarter of fiscal 2001 were comparable to revenues in the same quarter of the prior year. Management continues to believe that given the increased sophistication of Kronos' products and the related heightened need for pre-sales technological support and other sales support, the dealer channel's sales cycle requires greater management and participation by Kronos. To address this trend, management anticipates expending greater resources to assist the dealer channel in the short term and increasing Kronos' emphasis on direct sales in the longer term.

Service revenues for the third quarter of fiscal 2001 increased to \$35.6 million as compared to \$29.5 million in the third quarter of fiscal 2000. Service revenues for the first nine months of fiscal 2001 were \$101.3 million as compared to \$87.7 million for the first nine months of the prior year. Service revenues grew at a rate of 21% and 15% during the three and nine month periods ended June 30, 2001, respectively. The growth in service revenues in these periods reflects an increase in the level of professional services delivered due to more effective management of resources as compared to the same period in the prior year. The growth in service revenues in the third quarter of fiscal 2001 also reflects an increase in maintenance revenue from expansion of the installed base, increased level of services sold to the installed base and, to a lesser extent, incremental service revenues resulting from Kronos' acquisitions over the past four quarters. Service revenues grew at a rate of 27% and 37% in the three and nine month periods ended July 1, 2000, respectively. The unusually high service revenue growth rate experienced in these periods is attributable to an increase in maintenance revenue from expansion of the installed base due to the accelerated product revenue growth experienced in fiscal 1999 because of demand for new products and upgrades resulting from customers' Year 2000 compliance efforts. Also contributing to the growth in service revenues in these periods were an increase in the level of maintenance contracts and professional services accompanying new and upgrade sales as well as maintenance and professional service revenues resulting from Kronos' acquisitions, including the acquisition of its largest dealer territory in June 1999.

Gross Profit. Gross profit as a percentage of revenues was 63% and 61% in the three and nine month periods ended June 30, 2001, respectively, compared to 61% in each of the comparable periods in the prior year. The improvement in gross profit in the third quarter was attributable to increases in both product and service gross profit. Product gross profit as a percentage of product revenues was 79% and 77% in the three and nine month periods ended June 30, 2001, respectively, compared to 77% in each of the comparable periods in the prior year. The improvement in product gross profit is principally attributable to product mix. Software, which typically generates higher gross profit, comprised a greater proportion of product revenues in the three and nine month periods ended June 30, 2001 as compared to the same periods in the prior year. However, higher software development amortization and production costs due to lower hardware sales volume partially offset the effect of this favorable mix. Service gross profit as a percentage of service revenues was 46% and 44% in the three and nine month periods ended June 30, 2001, compared to 40% and 42% in the comparable periods of the prior year. The improvement in service gross profit is

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attributable to increased productivity in the service organization and a reduction in discretionary spending. The improvement in productivity is the result of leveraging investments in service systems and processes coupled with a reduction in headcount to better align costs with revenues.

Net Operating Expenses. Net operating expenses as a percentage of revenues were 55% and 56% for the three and nine month periods ended June 30, 2001, respectively, as compared to 53% for the comparable periods in the prior year. The increase in operating expenses in fiscal 2001 as compared to fiscal 2000 is principally attributable to increased program and infrastructure costs incurred to support increases in business volume and product development efforts. Also contributing to the increase in operating expenses was an increase in the amortization of intangible assets related to acquisitions and the recognition of various special charges related to termination of operations and a reduction in workforce. Sales and marketing expenses as a percentage of revenues were 35% in the three and nine month periods ended June 30, 2001 and July 1, 2000. Engineering, research and development expenses as a percentage of revenues were 12% in the three and nine month periods ended June 30, 2001 as compared to 11% in the comparable periods of the prior year. Engineering expenses of \$9.1 million and \$7.2 million in the third quarter of fiscal 2001 and 2000, respectively, are net of capitalized software development costs of \$3.0 million and \$2.4 million, respectively. Engineering expenses of \$25.4 million and \$21.8 million in the first nine months of fiscal 2001 and 2000, respectively, are net of capitalized software development costs of \$8.4 million and \$7.2 million, respectively. The growth in engineering, research and development expenses this year resulted from the continuing research, design and development of software and hardware technology, principally related to the Company's Workforce 4.0 product and the 4500 Terminal. General and administrative expenses as a percentage of revenues were 7% in the three and nine month periods ended June 30, 2001 and 6% and 7% for the comparable periods of the prior year. Amortization of intangible assets as a percentage of revenues was 2% and 3% in the three and nine month periods ended June 30, 2001 and July 1, 2000. The increase in amortization expense is principally related to various acquisitions completed in the past four quarters. Kronos amortizes these costs over the assets estimated remaining economic lives. Other income, net is principally attributable to interest income earned from Kronos' cash as well as investments in its marketable securities and lease portfolio.

Special Charge. A special charge in the amount of \$700,000 was recorded in the third quarter of fiscal 2001 related to termination costs from a reduction in workforce of approximately 90 employees. The charge is the result of management's effort to streamline operations to better align costs with expected revenues. Kronos anticipates making cash outlays of less than \$100,000 relating to this action over the next three months. In the second quarter of fiscal 2001 Kronos recorded a special charge in the amount of \$3.0 million related to the termination of Kronos' Crosswinds Technology operations. The Crosswinds Technology Group, which was purchased in May 1999, was responsible for the product development, marketing and sales support of time and attendance applications that operated as a Microsoft Outlook plug in product. Lower than anticipated sales of these applications, redundant infrastructure and ongoing operating losses resulted in the termination of the Crosswinds Technology Group as a stand-alone operating unit. The \$3.0 million charge consists of \$1.6 million in termination costs, \$1.3 million for the write off of intangible assets and \$100,000 in other costs. Cash outlays of approximately \$1.2 million relating to this action are anticipated to be paid over the next nine months. The anticipated pre-tax savings resulting from these actions is a cost reduction, principally salaries, of approximately \$1.9 million for the remainder of fiscal 2001 and \$7.5 million annually thereafter, excluding amortization of \$1.3 million over the next three years.

Income Taxes. The provision for income taxes as a percentage of pretax income was income tax was 35% in the three and nine month periods ended June 30,

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2001, respectively, as compared to 37% in the comparable periods of the prior year. The lower effective income tax rate experienced in fiscal 2001 was principally attributable to tax benefits resulting from Kronos' investment tax credits. Management anticipates the effective income tax rate for the remainder of the fiscal year will be 35%.

Newly Issued Accounting Standards. In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, "Business Combinations", and No. 142, "Goodwill and Other Intangible Assets", effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill (and intangible assets deemed to have indefinite lives) will no longer be amortized but will be subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives.

For acquisitions completed prior to June 30, 2001, the Company will apply the new rules on accounting for business combinations and goodwill and other intangible assets beginning in the first quarter of fiscal year 2002. For acquisitions completed after June 30, 2001, the Company will apply the new rules beginning in the fourth quarter of fiscal year 2001. The Company has not yet determined the effect that the application of the non-amortization provisions of the Statements will have on net income. During fiscal year 2002, the Company will perform the first of the required impairment tests of goodwill as of October 1, 2001 and has not yet determined what the effect of these tests will be on earnings and financial position of the Company.

Liquidity and Capital Resources

Working capital as of June 30, 2001, amounted to \$19.6 million as compared to \$10.7 million at September 30, 2000. During fiscal 2000, working capital was reduced as Kronos funded its investment in its corporate headquarters facility and other property, plant and equipment, as well as the repurchase of common shares under Kronos' stock repurchase program and, to a lesser extent, payments related to acquisitions. Cash, cash equivalents and marketable securities amounted to \$68.2 million as of June 30, 2001 and \$51.4 million as of September 30, 2000. Included in the cash balance as of June 30, 2001 was \$10.5 million that was held in escrow pending the completion of an acquisition in July 2001.

Cash generated from operations amounted to \$34.3 million in the first nine months of fiscal 2001 as compared to \$26.7 million in the first nine months of fiscal 2000. The increase in cash generated from operations is principally attributable to increased collection of accounts receivable as well as increased accrued compensation, partially offset by lower earnings and a smaller increase in deferred service revenues as compared to the prior year. Cash used for property, plant and equipment was \$4.6 million in the first nine months of fiscal 2001 compared to \$17.0 million in the same period of fiscal 2000. Fiscal 2000 investments in property, plant and equipment were principally related to the construction of Kronos' corporate headquarters campus as well as investments in information systems and infrastructure to improve and support expanded operations. Excess cash reserves not required for operations, investments in property, plant and equipment or acquisitions are invested in marketable securities. Marketable securities increased by \$19.5 million in fiscal 2001 compared to a decrease of \$12.6 million in the first nine months of fiscal 2000. Kronos' use of cash for the acquisition of businesses in the first nine months of fiscal year 2001 was principally related to the acquisition of a dealer territory in November 2000 and the April 2001 acquisition of a competing provider of labor management solutions located in Australia. These acquisitions did not have a material impact on revenues or results of operations in the three and nine months ended June 30, 2001. Subsequent to June 30, 2001 Kronos acquired substantially all of the assets of a competing provider of labor management solutions to the U.S. healthcare industry. Management does not anticipate that

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this acquisition will have a material impact on revenues or results of operations in the fourth quarter. 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.

Under Kronos' stock repurchase program, Kronos repurchased 171,000 common shares in the first nine months of fiscal 2001 at a cost of \$6 million compared to 494,000 common shares at a cost of \$21.4 million for the same period in the prior year. The common shares repurchased under the program are used for Kronos' employee stock option plans and employee stock purchase plan. Cash provided by operations was more than sufficient to fund investments in capitalized software development costs, property, plant and equipment and stock repurchases. Kronos believes it has adequate cash and investments and operating cash flow to fund its investments in property, plant and equipment, software development costs, cash payments related to acquisitions, if any, and any additional stock repurchases for the foreseeable future.

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 ability to attract and retain sufficient technical personnel, competitive pricing pressure, the dependence on Kronos' time and attendance product line, 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, 2000, which are specifically incorporated by reference herein.

Potential Fluctuations in Quarterly Results. Kronos' quarterly operating results may fluctuate as a result of a variety of factors, including the purchasing patterns of its customers, mix of products and services sold, the timing of the introduction of new products and product enhancements by Kronos and its competitors, 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 fourth quarter and a relatively smaller percentage in the first quarter of each fiscal year, although there can be no assurance that this pattern will continue. In addition, while Kronos has contracts to supply systems to certain customers over an extended period of time, 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 operating results for any one period are not necessarily indicative of results for any future period.

Product Development and Technological Change. Continual change and improvement in computer software and hardware technology characterize the markets for frontline 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

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needs of its customers. Although Kronos is continually seeking to further enhance its product offerings 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 Time and Attendance Product Line. To date, more than 90% of the Kronos' revenues have been attributable to sales of time and attendance systems and related services and Kronos expects that to continue in the next fiscal year. Competitive pressures or other factors could cause Kronos' time and attendance products to lose market acceptance or experience significant price erosion, adversely affecting the results of Kronos' operations.

Dependence on Alternate Distribution Channels. Kronos markets and sells its products through its direct sales organization, independent dealers and OEMs. In the first nine months of fiscal 2001, approximately 13% of Kronos' revenue was generated through sales to dealers and OEMs. A reduction in the sales efforts of Kronos' major dealers and/or OEMs, the termination or changes in their relationships with Kronos, or the failure of Kronos to monitor and incent its independent dealers and OEMs, could have a material adverse affect on the results of Kronos' operations.

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.

Competition. The frontline labor management industry is highly competitive. Technological changes such as those allowing for increased use of the Internet may also create the potential for new entrants. Although Kronos believes it has core competencies that are not easily obtainable by competitors, 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.

PART II. OTHER INFORMATION

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

None

(b) Reports on Form 8-K

There were no reports on Form 8-K filed during the fiscal quarter ended June 30, 2001.

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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

By /s/ Paul A. Lacy
 Paul A. Lacy
Vice President of Finance
 and Administration
(Duly Authorized Officer and
Principal Financial Officer)

August 10, 2001