

WATER PIK TECHNOLOGIES INC
Form 10-Q
November 13, 2002

[QuickLinks](#) -- Click here to rapidly navigate through this document

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2002

**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 1-15297

WATER PIK TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

25-1843384
(IRS Employer
Identification No.)

**23 Corporate Plaza, Suite 246
Newport Beach, CA 92660**

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: **(949) 719-3700**

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 No

The number of shares of Common Stock outstanding on November 11, 2002 was 12,447,865 shares.

WATER PIK TECHNOLOGIES, INC.

INDEX

Part I Financial Information

Item 1.	Consolidated Financial Statements	
	Consolidated Balance Sheets September 30, 2002 (unaudited) and December 31, 2001	3
	Consolidated Statements of Income Three months and nine months ended September 30, 2002 and 2001 (unaudited)	4
	Consolidated Statements of Cash Flows Nine months ended September 30, 2002 and 2001 (unaudited)	5
	Notes to Consolidated Financial Statements (unaudited)	6
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	13
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	23
Item 4.	Controls and Procedures	23
Part II Other Information		
Item 6.	Exhibits and Reports on Form 8-K	24
Signatures		
	Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	26

PART I FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

Water Pik Technologies, Inc.
Consolidated Balance Sheets

(In thousands, except for share and per share amounts)

	September 30, 2002	December 31, 2001
	(Unaudited)	
Assets		
Current assets:		
Cash	\$ 4,162	\$ 997
Accounts receivable, less allowances of \$2,322 at September 30, 2002 and \$2,623 at December 31, 2001	45,377	73,739
Inventories	44,144	33,227
Deferred income taxes	5,494	5,267
Prepaid expenses and other current assets	3,192	2,629
Total current assets	102,369	115,859
Property, plant and equipment, net	51,605	54,167
Goodwill, net	18,379	18,296

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	September 30, 2002	December 31, 2001
Intangible assets, net	538	809
Deferred income taxes	2,919	3,434
Other assets	1,797	2,026
Total assets	\$ 177,607	\$ 194,591
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 18,139	\$ 22,144
Accrued income taxes	351	2,721
Accrued liabilities	20,783	25,523
Current portion of long-term debt	2,918	4,722
Total current liabilities	42,191	55,110
Long-term debt, less current portion	33,455	41,923
Other accrued liabilities	6,419	7,448
Total liabilities	82,065	104,481
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value: 5,000,000 shares authorized; none issued		
Common stock, \$0.01 par value: 50,000,000 shares authorized; 12,444,865 and 12,245,677 shares issued and outstanding at September 30, 2002 and December 31, 2001, respectively	124	122
Additional paid-in capital	78,115	76,285
Retained earnings	26,780	21,516
Equity adjustments due to stock plans	(8,357)	(6,732)
Accumulated comprehensive loss	(1,120)	(1,081)
Total stockholders' equity	95,542	90,110
Total liabilities and stockholders' equity	\$ 177,607	\$ 194,591

See accompanying notes

3

Water Pik Technologies, Inc.
Consolidated Statements of Income

(In thousands, except for share and per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Sales	\$ 67,771	\$ 73,590	\$ 197,054	\$ 200,129
Cost and expenses:				
Cost of sales	45,578	50,607	134,424	137,060

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	Three Months Ended September 30,		Nine Months Ended September 30,	
Selling expenses	11,840	12,455	32,777	32,922
General and administrative expenses	4,719	5,049	13,783	15,138
Research and development expenses	2,469	1,889	6,154	5,898
	64,606	70,000	187,138	191,018
Income before other income and expenses	3,165	3,590	9,916	9,111
Interest expense	531	548	1,826	2,398
Other expense (income), net	201	(137)	(82)	(629)
Income before income taxes	2,433	3,179	8,172	7,342
Provision for income taxes	750	1,245	2,908	2,877
Net income	\$ 1,683	\$ 1,934	\$ 5,264	\$ 4,465
Basic net income per common share	\$ 0.14	\$ 0.16	\$ 0.44	\$ 0.38
Diluted net income per common share	\$ 0.13	\$ 0.16	\$ 0.42	\$ 0.37
Shares used in per share calculation basic	12,065,000	11,918,000	12,038,000	11,796,000
Shares used in per share calculation diluted	12,558,000	12,122,000	12,434,000	11,909,000

See accompanying notes

4

Water Pik Technologies, Inc.
Consolidated Statements of Cash Flows

(In thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2002	2001
Operating activities:		
Net income	\$ 5,264	\$ 4,465
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	7,700	7,011
Deferred income taxes	256	(78)
Compensation expense arising from stock awards	266	216
Loss (gain) on disposal of property, plant and equipment	468	(329)
Change in operating assets and liabilities:		
Accounts receivable	28,539	15,546
Inventories	(10,760)	(230)
Accounts payable	(4,052)	(5,554)

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	Nine Months Ended September 30,	
	2019	2018
Accrued liabilities	(4,716)	(4,017)
Accrued income taxes	(2,369)	(2,926)
Other assets and liabilities	(2,155)	(2,037)
Cash provided by operating activities	18,441	12,067
Investing activities:		
Purchases of property, plant and equipment	(5,270)	(13,956)
Disposals of property, plant and equipment	184	368
Cash used in investing activities	(5,086)	(13,588)
Financing activities:		
Net borrowings under revolving credit facilities	(8,567)	(9,562)
Payments on promissory notes	(1,647)	(3,210)
Net proceeds from common stock offering		13,646
Proceeds from exercise of options	78	
Principal payments on capital leases	(99)	(168)
Cash (used in) provided by financing activities	(10,235)	706
Effect of exchange rate changes on cash	45	(13)
Increase (decrease) in cash	3,165	(828)
Cash at beginning of period	997	1,383
Cash at end of period	\$ 4,162	\$ 555

See accompanying notes

5

Water Pik Technologies, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

DESCRIPTION OF BUSINESS

Water Pik Technologies, Inc. ("Water Pik Technologies" or the "Company") is a leader in designing, manufacturing and marketing a broad range of well-recognized personal health care products and pool products and water-heating systems. The Company's products include: showerheads; consumer and professional oral health products; water filtration products; personal stress relief products; home sanitizing products; swimming pool and spa heaters, electronic controls, valves, pumps, filters and water features; and residential and commercial water-heating systems. Water Pik Technologies operates in two business segments the Personal Health Care segment and the Pool Products and Heating Systems segment.

UNAUDITED INTERIM FINANCIAL INFORMATION

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Certain amounts reported in previous years have been reclassified to conform to the 2002 presentation. These reclassifications had no effect on reported results of operations or stockholders' equity. These financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2001. Operating results for the interim periods presented are not necessarily indicative of the results to be expected for the year ended December 31, 2002.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2002, The Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This statement requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Statement 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. Management does not expect that adoption of this standard will have a material effect on the Company's consolidated results of operations or financial position.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 61, Amendment of FASB No. 13, and Technical Corrections." This statement clarifies guidance related to the reporting of gains and losses from extinguishment of debt and resolves inconsistencies related to the required accounting treatment of certain lease modifications. The provisions of this statement related to extinguishment of debt become effective for financial statements issued for fiscal years beginning after May 15, 2002. The provisions of this statement related to lease modifications are effective for transactions occurring after May 15, 2002. Management does not expect that adoption of this standard will have a material effect on the Company's consolidated results of operations or financial position.

6

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." SFAS No. 144 retained substantially all of the requirements of SFAS No. 121 while resolving certain implementation issues. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001. Adoption of SFAS No. 144 in the first quarter of 2002 had no impact on the Company's consolidated results of operations or financial position.

In June 2001, the FASB issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting, and broadens the criteria for recording intangible assets apart from goodwill. Under SFAS No. 142, goodwill and intangible assets that have indefinite useful lives will no longer be amortized but will be tested at least annually for impairment. Intangible assets with finite useful lives will continue to be amortized over their useful lives. The goodwill test for impairment consists of a two-step process that begins with an estimation of the fair value of the reporting unit. The first step of the test is a screen for potential impairment and the second step measures the amount of impairment, if any. SFAS No. 142 requires an entity to complete the first step of the transitional goodwill impairment test within six months of adopting the statement. The Company adopted SFAS No. 142 in the first quarter of fiscal 2002. In accordance with SFAS No. 142, Water Pik Technologies identified two reporting units, the Personal Health Care segment and the Pool Products and Heating Systems segment, which constitute components of its business that include goodwill. The Company completed the first step of the transitional goodwill impairment test as of January 1, 2002 and has determined that the fair value of each of the reporting units exceeded the reporting unit's carrying amount, and no impairment was indicated.

The following table provides the Company's net income and net income per share had the non-amortization provisions of SFAS No. 142 been adopted for all periods presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
	(In thousands, except per share amounts)			
Net income, as reported	\$ 1,683	\$ 1,934	\$ 5,264	\$ 4,465
Add back: Goodwill amortization		429		1,290
Related income tax effect		(86)		(308)

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	Three Months Ended September 30,		Nine Months Ended September 30,	
Adjusted net income	\$ 1,683	\$ 2,277	\$ 5,264	\$ 5,447
Basic net income per common share:				
Net income per common share, as reported	\$ 0.14	\$ 0.16	\$ 0.44	\$ 0.38
Add back: Goodwill amortization, net of related income tax effect		0.03		0.08
Adjusted net income per common share	\$ 0.14	\$ 0.19	\$ 0.44	\$ 0.46
Diluted net income per common share:				
Net income per common share, as reported	\$ 0.13	\$ 0.16	\$ 0.42	\$ 0.37
Add back: Goodwill amortization, net of related income tax effect		0.03		0.09
Adjusted net income per common share	\$ 0.13	\$ 0.19	\$ 0.42	\$ 0.46

Other intangible assets of \$538,000 and \$809,000 (net of accumulated amortization of \$737,000 and \$616,000) at September 30, 2002 and December 31, 2001, respectively consist primarily of acquired

7

patent rights and customer lists, which are amortized on a straight-line basis over periods ranging from 2 to 7 years.

In the fourth quarter 2001, the Company adopted Emerging Issues Task Force ("EITF") Issue 00-14, "Accounting for Certain Sales Incentives," and EITF Issue 00-25, "Vendor Income Statement Characterization of Consideration from a Vendor to a Retailer," resulting in the reclassification of certain customer promotional payments and cooperative advertising arrangements from selling expenses to a reduction in sales. Sales and selling expenses for all prior periods were restated to conform to this presentation. This reclassification resulted in a decrease in sales and selling expenses of \$1,653,000 and \$4,763,000 for the three months and nine months ended September 30, 2001, respectively. These reclassifications had no effect on reported operating profit.

2. Inventories

Inventories are stated at the lower of cost (last-in, first-out ("LIFO") and first-in, first-out ("FIFO") cost methods) or market. Inventories consist of the following:

	September 30, 2002	December 31, 2001
(In thousands)		
Raw materials and supplies	\$ 18,244	\$ 15,674
Work-in-process	4,597	4,745
Finished goods	25,358	16,803
Total inventories at current cost	48,199	37,222
Less: Allowances to reduce current cost values to LIFO basis	(4,055)	(3,995)
Total inventories	\$ 44,144	\$ 33,227

Inventories determined using the LIFO cost method were \$39,399,000 at September 30, 2002 and \$27,901,000 at December 31, 2001, net of the respective LIFO reserves. The remainder of inventory was determined using the FIFO cost method.

3. Long-Term Debt

Long-term debt is comprised of the following:

	September 30, 2002	December 31, 2001
	(In thousands)	
Revolving credit facility	\$ 7,227	\$ 13,522
Canadian revolving credit facility		2,233
Mortgage notes payable	19,835	20,453
Promissory notes payable - equipment financing facility	9,261	10,290
Long-term obligations under capital leases	50	147
	36,373	46,645
Less: Current portion	(2,918)	(4,722)
Long-term debt	\$ 33,455	\$ 41,923

In January 2002, the Company entered into two interest rate swap agreements that effectively convert the variable rate interest on the promissory notes payable under the equipment financing facility to a fixed rate. Under these agreements, payments are made based on a fixed rate and received on a LIBOR based variable rate. Differentials to be paid or received under the agreements are recognized as interest expense. The interest rate swap agreements expire on January 1, 2007, which

8

coincides with the maturity date of the promissory notes. These interest rate swaps, which the Company has designated as cash flow hedging instruments, meet the specific hedge criteria under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. As such, changes in their fair values of \$208,000 and \$433,000 for the three months and nine months ended September 30, 2002, respectively, have been recognized in accumulated comprehensive loss within stockholders' equity.

The counterparty to these interest rate swap agreements is a major financial institution. The Company continually monitors the credit quality of the financial institution and anticipates full performance by the counterparty.

The revolving credit facility, Canadian revolving credit facility and the real estate loan agreement and related mortgage notes require the Company to be in compliance with specific financial and non-financial covenants and restrictions. The Company was in compliance with these covenants at September 30, 2002.

4. Stock Option Fair Value Disclosure

The Company has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," but applies Accounting Principles Board ("APB") Opinion No. 25 and related interpretations in accounting for its plans. If the Company had elected to recognize compensation cost for its stock option plans based on the fair value at the grant dates for awards under the plans consistent with SFAS No. 123, net income and net income per common share would have been as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net income:				
As reported	\$ 1,683	\$ 1,934	\$ 5,264	\$ 4,465

(In thousands, except per share amounts)

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

the effective tax rate in 2002 is due to adjustments to rates utilized for the determination of the effective tax rate based on completion of prior year tax returns and to the non-amortization of goodwill for financial reporting purposes upon adoption of SFAS No. 142 effective January 1, 2002.

8. Legal Contingencies

A number of lawsuits, claims and proceedings have been or may be asserted against the Company relating to the conduct of its business, including those pertaining to product liability, personal injury, patent infringement, commercial, employment and employee benefits. While the outcome of litigation cannot be predicted with certainty and some of these lawsuits, claims or proceedings may be determined adversely to the Company, management does not believe that the disposition of any such pending matters is likely to have a material adverse effect on the Company's financial condition or liquidity, although the resolution in any reporting period of one or more of these matters could have a material adverse effect on the Company's results of operations for that period and ultimately could affect the Company's insurance premiums or its ability to obtain insurance coverage.

As a consumer goods manufacturer and distributor, the Company is subject to continuing risk of product liability and related lawsuits involving claims for substantial monetary damages. The Company is party to various personal injury and property damage lawsuits and claims relating to its products and other litigation incidental to its business. The Company has general liability, product liability and workers' compensation insurance coverage. The Company's insurance coverage provides that the

10

Company is responsible for policy deductibles and legal costs and expenses. Loss accruals have been recorded in accordance with SFAS No. 5, "Accounting for Contingencies" to cover the portion of general liability, product liability and workers' compensation claims, both asserted claims and incurred but not reported claims, that are not covered by insurance policies. Such accruals are based on estimates which include information provided by the Company's insurance company, claims adjusters and insurance broker, taking into account prior experience, numbers of claims, discussions with legal counsel and other relevant factors. The methods of making such estimates and establishing the resulting accrual are reviewed on a regular basis and any adjustments are reflected in current operating results.

The Company has recorded loss accruals covering the portion of lawsuits and claims not covered by insurance policies of \$5,821,000 and \$7,361,000 as of September 30, 2002 and December 31, 2001, respectively. The amount related to product and general liability lawsuits and asserted claims and incurred but not reported claims was \$4,736,000 and \$6,680,000 as of September 30, 2002 and December 31, 2001, respectively. The amount related to workers' compensation asserted claims and incurred but not reported claims was \$1,085,000 and \$681,000 as of September 30, 2002 and December 31, 2001, respectively.

In connection with the spin-off of Water Pik Technologies, Inc. from Allegheny Teledyne Incorporated, now known as Allegheny Technologies Incorporated ("ATI"), on November 29, 1999, ATI received a tax ruling from the Internal Revenue Service (the "IRS") stating that the spin-off would be tax-free to ATI and to ATI's stockholders. The Tax Sharing and Indemnification Agreement between the Company and ATI provides that the Company will indemnify ATI and its directors, officers, agents and representatives for any taxes imposed on, and other amounts paid by, them or ATI's stockholders if the Company takes actions or fails to take actions, that result in the spin-off not qualifying as a tax-free distribution. The significant restrictions imposed by the Tax Sharing and Indemnification Agreement expired on November 29, 2001 and the remaining restrictions expire on January 3, 2003. If any of the taxes or other amounts were to become payable by the Company, the payment could have a material adverse effect on the Company's business, results of operations, financials condition and cash flow.

9. Net Income Per Share

Basic net income per common share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share is calculated by dividing net income by the sum of the weighted average number of common shares outstanding plus the dilutive effect of unvested restricted shares and outstanding stock options using the "treasury stock" method.

A reconciliation of weighted average shares outstanding, used to calculate basic net income per common share, to weighted average shares outstanding assuming dilution, used to calculate diluted net income per common share, is as follows:

Three Months Ended September 30,		Nine Months Ended September 30,	
2002	2001	2002	2001

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	Three Months Ended September 30,		Nine Months Ended September 30,	
	(In thousands)			
Weighted average common shares outstanding basic	12,065	11,918	12,038	11,796
Diluted effect of employee stock options and restricted shares	493	204	396	113
Weighted average common shares outstanding diluted	12,558	12,122	12,434	11,909

11

10. Business Segments

The Company operates in two business segments organized around its products: the Personal Health Care segment and the Pool Products and Heating Systems segment. The Personal Health Care segment designs, manufactures and markets personal health care products, including showerheads, consumer and professional oral health products, water filtration products, personal stress relief products, and home sanitizing products. The Pool Products and Heating Systems segment designs, manufactures and markets swimming pool and spa heaters, electronic controls, valves, pumps, filters, water features and residential and commercial water-heating systems.

Information on the Company's business segments is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
	(In thousands)			
Sales:				
Personal Health Care	\$ 33,248	\$ 32,776	\$ 90,074	\$ 86,504
Pool Products and Heating Systems	34,523	40,814	106,980	113,625
Total sales	\$ 67,771	\$ 73,590	\$ 197,054	\$ 200,129
Operating profit:				
Personal Health Care	\$ 2,074	\$ 237	\$ 4,788	\$ 1,891
Pool Products and Heating Systems	1,091	3,353	5,128	7,220
Total operating profit	3,165	3,590	9,916	9,111
Interest expense	531	548	1,826	2,398
Other expense (income)	201	(137)	(82)	(629)
Income before income taxes	\$ 2,433	\$ 3,179	\$ 8,172	\$ 7,342
	September 30, 2002		December 31, 2001	
	(In thousands)			
Identifiable assets:				
Personal Health Care	\$	76,412	\$	69,849

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	September 30, 2002	December 31, 2001
Pool Products and Heating Systems	89,612	112,828
Corporate	11,583	11,914
Total identifiable assets	\$ 177,607	\$ 194,591

Total international sales were \$10,701,000 and \$32,928,000 for the three months and nine months ended September 30, 2002, respectively, and \$11,604,000 and \$33,552,000 for the three months and nine months ended September 30, 2001, respectively. Of these amounts, sales by operations in the United States to customers in other countries amounted to \$3,841,000 and \$11,744,000 for the three months and nine months ended September 30, 2002, respectively, and \$4,217,000 and \$12,069,000 for the three months and nine months ended September 30, 2001, respectively.

12

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis contains forward-looking statements regarding future events or the future financial performance of the Company that involve certain risks and uncertainties which are discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2001. Actual events or the actual future results of the Company may differ materially from any forward-looking statement due to such risks and uncertainties.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses Water Pik Technologies' consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, management evaluates its estimates and judgments. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies, among others, affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

REVENUE RECOGNITION

The Company recognizes revenue when persuasive evidence of a sales arrangement exists, delivery has occurred or services have been rendered, the buyer's price is fixed or determinable and collection is reasonably assured. The Company records estimated reductions to revenue for customer programs and incentive offerings including promotions, cooperative advertising programs and other volume-based incentives. Should the costs under these customer programs and incentive offerings exceed those estimated by the Company, additional reductions to revenue may be required. The Company also allows credit for products returned within its policy terms. The Company records an allowance for estimated returns, based on historical experience, at the time of sale. Should the actual returns exceed those estimated by the Company, additional reductions to revenue and cost of sales may be required.

ACCOUNTS RECEIVABLE

The Company markets its products to a diverse customer base, principally throughout the United States and Canada. The Company grants credit terms in the normal course of business to its customers. Additionally, the Company offers extended payment terms to pool products customers to encourage them to purchase products generally during the fourth quarter to better enable utilization of manufacturing capacity. The

Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined through review of their current credit information. The Company continuously monitors collections and payments from customers and maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Estimated losses are based on historical experience and any specific customer collection issues identified. If the financial condition of the Company's customers, including one customer, SCP Pool Corporation, accounting for approximately 6 and 27 percent of accounts receivable at September 30, 2002 and December 31, 2001, respectively, were

to deteriorate, resulting in an impairment of their ability to make payments, additional allowances and related bad debt expense may be required.

INVENTORIES

The Company values its inventory at the lower of the cost to purchase and/or manufacture the inventory (last-in, first-out ("LIFO") and first-in first-out ("FIFO") cost methods) or the current estimated market value of the inventory. The Company writes down its inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. This can occur if there is a decline in demand for the Company's existing products or if the market does not accept the Company's new or enhanced products, particularly when the product does not have a well-established market such as for the new Aquia home sanitizing system that incorporates ozone-generation technology. Market acceptance of new products is regularly evaluated after product launch. Generally, following introduction of a new product the Company allows 18 months, depending on the product category, before evaluating whether new product inventory should be written down as obsolete or unmarketable. If actual future demand or market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

WARRANTIES

The Company provides for the estimated cost of product warranties based on historical experience and any identified product quality issues at the time revenue is recognized. While the Company has comprehensive product quality programs and processes, including extensive testing during the new product development process and active monitoring and evaluation of its component suppliers, the warranty obligation is affected by product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from the Company's estimates, revisions to the estimated warranty liability may be required.

DEFERRED INCOME TAXES

The Company has not recorded a valuation allowance on its deferred tax assets as management believes that it is more likely than not that all deferred tax assets will be realized. While the Company has considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event the Company were to determine that it would not be able to realize all or part of its net deferred tax assets in the future, an adjustment to the deferred tax assets would be charged to income in the period such determination was made.

PROPERTY, PLANT AND EQUIPMENT

The Company states property, plant and equipment at cost less accumulated depreciation and amortization. Depreciation and amortization are determined using a combination of accelerated and straight-line methods over the estimated useful lives of the various asset classes. The Company estimates the useful lives of property, plant and equipment based on historical experience and estimates of future demand and market conditions. Should the actual useful lives be less than those estimated, additional depreciation expense may be required.

LONG-LIVED ASSETS IMPAIRMENT

The Company currently evaluates long-lived assets, including goodwill and other intangibles, for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. In assessing the recoverability of long-lived assets, including goodwill and other

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

intangible assets, the Company must make assumptions regarding estimated future cash flows and other factors to determine the fair value of the respective assets. If these estimates or their related assumptions change in the future, the Company may be required to record impairment charges for these assets.

INSURANCE RESERVES AND LEGAL CONTINGENCIES

The Company records loss accruals to cover the portion of general liability, product liability and workers' compensation claims, both asserted claims and incurred but not reported claims, that are not covered by insurance policies. Such accruals are estimated based on information provided by the Company's insurance company, claims adjusters and insurance broker, taking into account prior experience, numbers of claims, discussions with legal counsel and other relevant factors. Should the number of claims or the actual outcome of any claim result in losses in excess of amounts accrued, an adjustment to the loss accruals and increase in expense may be required.

Overview of Business

Water Pik Technologies is a leader in designing, manufacturing and marketing a broad range of well-recognized personal health care products and pool products and water-heating systems. The Company operates in two business segments: the Personal Health Care segment and the Pool Products and Heating Systems segment. The Personal Health Care segment designs, manufactures and markets personal health care products, including showerheads, consumer and professional oral health products, water filtration products, personal stress relief products and home sanitizing products. The Pool Products and Heating Systems segment designs, manufactures and markets swimming pool and spa heaters, electronic controls, valves, pumps, filters, water features and residential and commercial water-heating systems.

Results of Operations

Consolidated sales by segment and results of operations for the three months and nine months ended September 30, 2002 and 2001 are summarized below:

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2002	2001	% Change	2002	2001	% Change
(Dollars in thousands)						
Sales:						
Personal Health Care	\$ 33,248	\$ 32,776		\$ 90,074	\$ 86,504	
Pool Products and Heating Systems	\$ 34,523	\$ 40,814		\$ 106,980	\$ 113,625	
Total sales	\$ 67,771	\$ 73,590	(7.9)%	\$ 197,054	\$ 200,129	(1.5)%
Gross profit	\$ 22,193	\$ 22,983	(3.4)%	\$ 62,630	\$ 63,069	(0.7)%
Operating profit	\$ 3,165	\$ 3,590	(11.8)%	\$ 9,916	\$ 9,111	8.8%
Gross profit as a percentage of sales	32.7%	31.2%		31.8%	31.5%	
Operating profit as a percentage of sales	4.7%	4.9%		5.0%	4.6%	
International sales as a percentage of sales	15.8%	15.8%		16.7%	16.8%	

Three months ended September 30, 2002 compared to the three months ended September 30, 2001

Sales for the three months ended September 30, 2002 were \$67,771,000, representing a decrease of \$5,819,000 over the comparable period in 2001, due to lower sales in the Pool Products and Heating Systems segment. Gross profit (sales less cost of sales) decreased \$790,000 to \$22,193,000 for the three months ended September 30, 2002 due to the decrease in sales. Gross profit as a percentage of sales

increased to 32.7 percent for the three months ended September 30, 2002 as compared to 31.2 percent for the same period of 2001. The impact of an improvement in the gross profit percentage in the Personal Health Care segment was partially offset by a slight deterioration in the gross profit percentage in the Pool Products and Heating Systems segment due primarily to a decrease in pool product sales. The gross profit percentage was also favorably impacted by a product mix shift in 2002 to more profitable Personal Health Care products.

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

Operating profit (gross profit less selling, general and administrative, and research and development expenses) decreased \$425,000 or 11.8 percent to \$3,165,000 for the three months ended September 30, 2002 from \$3,590,000 for the three months ended September 30, 2001. The decrease is due to the decrease in gross profit of \$790,000 as discussed above partially offset by a decrease in operating expenses of \$365,000. The decrease in operating expenses is due to a \$615,000 decrease in selling expenses, which were higher in 2001 due to activities related to new product introductions, and to a \$430,000 decrease in goodwill amortization upon adoption in the first quarter 2002 of the new accounting policy on goodwill and other intangible assets, which no longer permits the amortization of goodwill, partially offset by increased research and development expenses related to new product development activities.

Interest expense, which relates to borrowings under the Company's credit facilities and to promissory and mortgage notes payable decreased \$17,000 to \$531,000 for the three months ended September 30, 2002 from \$548,000 for the three months ended September 30, 2001 due to lower weighted average interest rates on borrowings during the three months ended September 30, 2002 as compared with the same period of 2001.

The effective income tax rate was 30.8 percent for the three months ended September 30, 2002 as compared with 39.2 percent for the comparable period of 2001. The 2002 effective income tax rate reflects adjustments to rates utilized for the determination of the effect tax rate based upon completion of prior year tax returns. The decrease in the effective income tax rate was also due to the non-amortization of goodwill for financial reporting purposes upon adoption in the first quarter 2002 of the new accounting policy on goodwill and other intangible assets.

Nine months ended September 30, 2002 compared to the nine months ended September 30, 2001

Sales for the nine months ended September 30, 2002 were \$197,054,000, representing a decrease of \$3,075,000 or 1.5 percent over the comparable period in 2001, due to lower sales in the Pool Products and Heating Systems segment partially offset by an increase in Personal Health Care segment sales. Gross profit decreased \$439,000 to \$62,630,000 for the nine months ended September 30, 2002 due to the decrease in sales. Gross profit as a percentage of sales was 31.8 percent for the nine months ended September 30, 2002 compared to 31.5 percent for the same period in 2001. The gross profit percentage was favorably impacted by a product mix shift in 2002 to more profitable Personal Health Care products as compared to 2001.

Operating profit increased \$805,000 to \$9,916,000 for the nine months ended September 30, 2002 from \$9,111,000 for the nine months ended September 30, 2001. The increase in operating profit is due to a decrease in operating expenses of \$1,244,000 partially offset by the decrease in gross profit as discussed above. General and administrative expenses decreased \$1,355,000 to \$13,783,000 for the nine months ended September 30, 2002 from \$15,138,000 for the same period of 2001 primarily due to a decrease in goodwill amortization of \$1,290,000.

Interest expense decreased \$572,000 to \$1,826,000 for the nine months ended September 30, 2002 from \$2,398,000 for the nine months ended September 30, 2001. This decrease is due to lower weighted average interest rates on borrowings during the nine months ended September 30, 2002 as compared with the same period of 2001 partially offset by higher average borrowings outstanding during 2002 as compared to 2001.

16

The effective income tax rate was 35.6 percent for the nine months ended September 30, 2002 as compared with 39.2 percent for the comparable period of 2001. The 2002 effective income tax rate reflects adjustments to rates utilized for the determination of the effect tax rate based upon completion of prior year tax returns. The decrease in the effective income tax rate was also due to the non-amortization of goodwill for financial reporting purposes upon adoption in the first quarter 2002 of the new accounting policy on goodwill and other intangible assets.

Personal Health Care Results of Operations

Personal Health Care segment sales by major category and segment consolidated results of operations for the three months and nine months ended September 30, 2002 and 2001 are summarized below. The other products category includes personal stress relief products, water filtration products and home sanitizing products.

Three Months Ended September 30,			Nine Months Ended September 30,		
2002	2001	% Change	2002	2001	% Change

(Dollars in thousands)

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

	Three Months Ended September 30,			Nine Months Ended September 30,		
Sales:						
Oral health products	\$ 13,482	\$ 14,032		\$ 37,184	\$ 38,214	
Shower products	\$ 14,388	\$ 15,853		\$ 42,779	\$ 39,366	
Other products	\$ 5,378	\$ 2,891		\$ 10,111	\$ 8,924	
Total sales	\$ 33,248	\$ 32,776	1.4%	\$ 90,074	\$ 86,504	4.1%
Gross profit	\$ 13,485	\$ 12,250	10.1%	\$ 35,044	\$ 33,523	4.5%
Operating profit	\$ 2,074	\$ 237	775.1%	\$ 4,788	\$ 1,891	153.2%
Gross profit as a percentage of sales	40.6%	37.4%		38.9%	38.8%	
Operating profit as a percentage of sales	6.2%	0.7%		5.3%	2.2%	
International sales as a percentage of sales	17.1%	18.4%		17.5%	18.7%	

Three months ended September 30, 2002 compared to the three months ended September 30, 2001

Sales in the Personal Health Care segment for the three months ended September 30, 2002 were \$33,248,000, an increase of \$472,000 or 1.4 percent over the comparable period in 2001. Increased sales of personal stress relief products, including sales of foot spas introduced in 2001 and of the AccuReach precision massager introduced in third quarter 2002, were partially offset by decreased sales of consumer oral health products, primarily oral irrigators, and decreased shower products sales. Increased sales of new shower products, including the New Visions® shower products introduced in 2001 and the Full-Body Shower Panel introduced in third quarter 2002, were offset by decreased sales of other shower products lines. Personal Health Care segment sales for the three months ended September 30, 2002 were also favorably impacted by lower payments on prior year sales incentive programs than originally estimated.

Gross profit increased \$1,235,000 to \$13,485,000 for the three months ended September 30, 2002 from \$12,250,000 for the comparable period in 2001. Gross profit as a percentage of sales for the three months ended September 30, 2002 increased to 40.6 percent from 37.4 percent primarily due to higher 2001 freight costs incurred to expedite new sourced products and to the favorable impact from sales allowances partially offset by increased depreciation expense on capital expenditures for new products.

Operating profit increased \$1,837,000 to \$2,074,000 for the three months ended September 30, 2002 from \$237,000 for the three months ended September 30, 2001. Operating profit as a percentage of sales increased to 6.2 percent for the three months ended September 30, 2002 from 0.7 percent for the three months ended September 30, 2001. The improvement in operating profit is due to the

17

increase in gross profit and to a decrease in selling expenses, which were higher in 2001 due to activities related to new product introductions.

Nine months ended September 30, 2002 compared to the nine months ended September 30, 2001

Sales in the Personal Health Care segment for the nine months ended September 30, 2002 were \$90,074,000, an increase of \$3,570,000 or 4.1 percent over the comparable period in 2001. Increased shower products sales, including sales of the Cascadia®, AquaFall® and New Visions® showerheads introduced in 2001 and sales of the new Full-Body Shower Panel introduced in third quarter 2002, and increased personal stress relief products, including sales of foot spas introduced in 2001 and of the AccuReach precision massager introduced in third quarter 2002, were partially offset by decreased sales of water filtration products and consumer oral health products.

Gross profit increased \$1,521,000 to \$35,044,000 for the nine months ended September 30, 2002 from \$33,523,000 for the comparable period in 2001 due to the increase in sales partially offset by increased depreciation expense related to capital expenditures for new products introduced in 2001 and 2002. Gross profit as a percentage of sales for the nine months ended September 30, 2002 was comparable to the gross profit for the same period in 2001.

Operating profit increased \$2,897,000 to \$4,788,000 for the nine months ended September 30, 2002 from \$1,891,000 for the nine months ended September 30, 2001. Operating profit as a percentage of sales increased to 5.3 percent for the nine months ended September 30, 2002 from 2.2 percent for the same period of 2001. The improvement in operating profit is due to increased gross profit and to decreased selling and research and development expenses. The decrease in selling and research and development expenses is due to elevated product development and introduction activities in 2001 related to new products introduced in 2001 and 2002.

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

Pool Products and Heating Systems Results of Operations

Pool Products and Heating Systems segment sales by major category and segment consolidated results of operations for the three months and nine months ended September 30, 2002 and 2001 are summarized below.

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2002	2001	% Change	2002	2001	% Change
(Dollars in thousands)						
Sales:						
Pool products	\$ 25,836	\$ 30,278		\$ 82,457	\$ 86,764	
Water-heating systems	\$ 8,687	\$ 10,536		\$ 24,523	\$ 26,861	
Total sales	\$ 34,523	\$ 40,814	(15.4)%	\$ 106,980	\$ 113,625	(5.8)%
Gross profit	\$ 8,708	\$ 10,733	(18.9)%	\$ 27,586	\$ 29,546	(6.6)%
Operating profit	\$ 1,091	\$ 3,353	(67.5)%	\$ 5,128	\$ 7,220	(29.0)%
Gross profit as a percentage of sales	25.2%	26.3%		25.8%	26.0%	
Operating profit as a percentage of sales	3.2%	8.2%		4.8%	6.4%	
International sales as a percentage of sales	14.6%	13.7%		16.1%	15.2%	

Three months ended September 30, 2002 compared to the three months ended September 30, 2001

Sales in the Pool Products and Heating Systems segment decreased \$6,291,000 or 15.4 percent to \$34,523,000 for the three months ended September 30, 2002 from \$40,814,000 for the comparable period of 2001. Pool products sales decreased \$4,442,000 primarily due to the accelerated timing of shipments related to seasonal selling programs in 2001. Water-heating system sales decreased \$1,849,000

18

primarily due to a general decline in the economy and increased competitive pressure in commercial markets.

Gross profit decreased \$2,025,000 to \$8,708,000 for the three months ended September 30, 2002 from \$10,733,000 for the comparable period of 2001 due to the sales decrease. Gross profit as a percentage of sales decreased to 25.2 percent for the three months ended September 30, 2002 from 26.3 percent for the same period in 2001 due to the lower sales volume resulting in fixed manufacturing costs representing a higher percentage of sales and to a product mix shift to lower margin products.

Operating profit decreased \$2,262,000 to \$1,091,000 for the three months ended September 30, 2002 from \$3,353,000 for the three months ended September 30, 2001. Operating profit as a percentage of sales decreased to 3.2 percent for the three months ended September 30, 2002 from 8.2 percent in the comparable period of 2001. The decrease in operating profit is due primarily to the decline in sales as well as to increased research and development expenses related to new product development activities partially offset by a \$416,000 decrease in goodwill amortization.

Nine months ended September 30, 2002 compared to the nine months ended September 30, 2001

Sales in the Pool Products and Heating Systems segment were \$106,980,000 for the nine months ended September 30, 2002, a decrease of \$6,645,000 or 5.8 percent from the comparable period of 2001. The decrease consists of a \$4,307,000 decrease in pool products sales, due to the accelerated timing of shipments related to seasonal selling programs in 2001, and to a \$2,338,000 decrease in water-heating systems sales, due to a general decline in the economy and increased competitive pressure in commercial markets.

Gross profit decreased \$1,960,000 to \$27,586,000 for the nine months ended September 30, 2002 from \$29,546,000 for the same period in 2001 due to the decline in sales. Gross profit as a percentage of sales decreased to 25.8 percent for the nine months ended September 30, 2002 from 26.0 percent for the same period in 2001.

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

Operating profit decreased \$2,092,000 to \$5,128,000 for the nine months ended September 30, 2002 from \$7,220,000 in the comparable period of 2001 primarily due to the decline in sales, to increased selling expenses and to increased research and development expenses related to new product development activities partially offset by a \$1,251,000 decrease in goodwill amortization.

Seasonality

The Company's business is highly seasonal, with operating results varying from quarter to quarter. The Personal Health Care segment has historically experienced higher sales in the fourth quarter of each year due to stronger retail demand during the holiday season. The Pool Products and Heating Systems segment has historically experienced higher sales in the second and fourth quarters of each year as customers purchase such products in preparation for the cooler weather and in anticipation of the warm spring and summer months. In addition, as a result of the seasonality of sales, the Pool Products and Heating Systems segment offers incentive programs and extended payment terms to encourage pool product customers to purchase products generally during the fourth quarter, as is consistent with industry practice. Seasonal variations in operating results can also occur due to short-term trends such as changes in the economic environment and weather patterns.

Financial Condition and Liquidity

The Company's principal capital requirements are to fund working capital needs and capital expenditures and to meet required debt payments. The Company anticipates that its operating cash flow, together with available borrowings under the credit facilities described below, will be sufficient to meet working capital requirements, fund capital expenditures and make scheduled principal and

19

interest payments on its debt obligations for at least the next 12 months. However, a decrease in demand for the Company's products or deterioration in the Company's financial ratios under its credit facilities could adversely affect its liquidity.

Cash increased \$3,165,000 from \$997,000 at December 31, 2001 to \$4,162,000 at September 30, 2002. Cash provided by operating activities of \$18,441,000 was used to repay borrowings under the Company's credit facilities of \$8,567,000, to make scheduled payments on promissory notes of \$1,647,000 and to fund capital expenditures of \$5,270,000.

Net cash provided by operations during the nine months ended September 30, 2002 results primarily from net income adjusted for non-cash items including depreciation and amortization expense and from collections of accounts receivable balances that are seasonally higher at year-end. This was partially offset by decreases in accrued liabilities, income taxes and accounts payable and from an increase in inventory. The decrease in accrued liabilities is primarily due to the payment of customer rebates, bonuses and commissions accrued for 2001 during first quarter 2002. The decrease in income taxes payable from December 31, 2001 to September 30, 2002 is due to the payment in first quarter 2002 of estimated taxes for the 2001 tax year as well as to payments of estimated 2002 taxes. The decrease in accounts payable results from payments in first quarter 2002 on higher year-end balances that result from increased production for seasonally higher fourth quarter sales. The increase in inventory is due to new product inventory including the Aquia sanitizing system and New Visions® showerhead, which had lower than anticipated sales, and to the build-up of the new AccuReach massager inventory and other inventory in preparation for seasonally strong sales in the third and fourth quarters.

For the nine months ended September 30, 2001, cash provided by operating activities of \$12,067,000 and the net proceeds of \$13,646,000 from issuance of common stock were used to fund capital expenditures of \$13,956,000 and for repayment of a promissory note and borrowings under the Company's credit facilities.

The Company's working capital was \$60,178,000 at September 30, 2002 as compared to \$60,749,000 at December 31, 2001. The decrease in working capital is primarily due to the decrease in accounts receivable partially offset by increases in cash and inventory and decreases in accounts payable, accrued income taxes, accrued liabilities and current portion of long-term debt. These fluctuations are reflective of the seasonality of the Company's businesses. Working capital was \$46,481,000 at September 30, 2001. The increase in working capital from September 30, 2001 to September 30, 2002 is primarily due to increased inventory and to increased cash at the Company's Canadian subsidiary. The increase in inventory is due to new product inventory including the Aquia sanitizing system and New Visions® showerhead, which had lower than anticipated sales, to the build-up of the new AccuReach massager inventory and other inventory in preparation for seasonally strong sales in the third and fourth quarters, and to the timing of shipments under seasonal selling programs. The current ratio increased to 2.4 at September 30, 2002 from 2.1 at September 30, 2001 and December 31, 2001.

The Aquia home sanitizing system was introduced in the fourth quarter of 2001 to retail, catalog and infomercial markets with limited success. The Company is currently pursuing international consumer and domestic commercial markets including medical offices, restaurants and day care centers through third party distributors. The Company has received its first international order to be shipped in the fourth quarter 2002.

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

If these efforts are not successful, the Company may be required to write down up to \$2,452,000 in remaining net inventory.

The Company has general liability, product liability and workers' compensation insurance programs. Insurance coverage under these programs are subject to policy deductibles for which the Company is at risk for losses. The actual settlements or other resolution of claims under these insurance programs may differ from estimated reserves, but the possible range of loss in excess of those accrued is not reasonably estimable. Based upon currently available information, management does not

20

believe that resolution of any pending insurance claims will have a material adverse effect on the Company's financial condition, results of operations or liquidity although the resolution in any reporting period of one or more of these matters could have a material adverse effect on the Company's results of operations for that period and ultimately could affect the Company's insurance premiums or its ability to obtain insurance coverage.

In connection with the spin-off, ATI received a tax ruling from the IRS stating that the spin-off would be tax-free to ATI and to ATI's stockholders. The Tax Sharing and Indemnification Agreement between the Company and ATI provides that the Company will indemnify ATI and its directors, officers, agents and representatives for any taxes imposed on, and other amounts paid by, them or ATI's stockholders if the Company takes actions or fails to take actions, that result in the spin-off not qualifying as a tax-free distribution. The significant restrictions imposed by the Tax Sharing and Indemnification Agreement expired on November 29, 2001 and the remaining restrictions expire on January 3, 2003. If any of the taxes or other amounts were to become payable by the Company, the payment could have a material adverse effect on the Company's business, results of operations, financials condition and cash flow.

The Company has a \$60,000,000 revolving bank credit facility that expires in November 2004. Borrowings under the facility are limited to borrowing base calculations based upon eligible accounts receivable and inventory balances. The credit facility also provides for the issuance of letters of credit up to the borrowing base less the outstanding line of credit, not to exceed \$10,000,000. At September 30, 2002, there were \$7,227,000 in borrowings and \$4,883,000 in letters of credit outstanding under the credit facility with \$22,043,000 of borrowing availability remaining under borrowing base limitations of the credit facility.

The Company's Canadian subsidiary has a CDN. \$11,000,000 revolving bank line of credit facility, increasing by CDN. \$1,000,000 for certain months of the year, a forward exchange contract facility of up to CDN. \$2,000,000 and a letter of credit facility of up to CDN. \$500,000. Borrowings under the facility are due on demand. At September 30, 2002, there were no borrowings or letters of credit outstanding under the credit facility and CDN. \$4,744,000 (US \$3,046,000) of borrowing availability remaining under borrowing base limitations of the credit facility.

On October 22, 2001, the Company entered into a real estate financing agreement with a bank and mortgaged its four U.S. manufacturing facilities to secure four promissory notes totaling \$20,590,000. The notes bear interest at LIBOR (London Interbank Offered Rate) plus 150 to 250 basis points per annum. The notes require monthly payments of approximately \$69,000 plus accrued interest through August 2008 with a final principal payment of \$14,893,000 and accrued interest due on September 30, 2008. The balance outstanding at September 30, 2002 was \$19,835,000.

On December 21, 2001, the Company entered into a \$15,000,000 equipment financing agreement with a bank. Initial borrowings under the agreement of \$10,290,000 were funded on December 28, 2001 and are evidenced by two term notes secured by specific machinery and equipment located at the Company's manufacturing facilities. The notes require quarterly payments of \$514,500 plus accrued interest beginning on April 1, 2002 with all unpaid principal balances and accrued interest due on January 1, 2007. The balance outstanding at September 30, 2002 was \$9,261,000. In January 2002, the Company entered into interest rate swap agreements that effectively convert the variable rate interest on the \$10,290,000 promissory notes payable to a fixed rate of 6.73 percent. The interest rate swap expires on January 1, 2007. Interest differentials to be paid or received because of the swap agreements are reflected as an adjustment to interest expense over the related period that the debt is outstanding. In fourth quarter 2002, the Company borrowed an additional \$4,500,000 under the facility evidenced by two term notes secured by specific machinery and equipment located at the Company's manufacturing facilities. The notes require quarterly payments of \$225,000 beginning on December 29, 2002 with all

21

unpaid principal balances and accrued interest due on September 30, 2007. No additional amounts can be borrowed under this facility.

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

The Company's revolving credit facilities and mortgage notes payable require it or its subsidiaries to comply with various financial covenants and restrictions, including covenants and restrictions relating to indebtedness, liens, investments, dividend payments, consolidated net worth, interest coverage, fixed charge coverage, capital expenditures and the relationship of the Company's total consolidated indebtedness to its earnings before interest, taxes, depreciation and amortization. A security interest in substantially all of the Company's assets was granted as collateral to the lenders under the credit agreements. To the extent that the Company is not able to comply with the financial covenants, it may be unable to borrow additional amounts and outstanding amounts may become due on an accelerated basis, which would adversely affect the Company's liquidity.

Due to the seasonality of the Company's pool products business, the extended payment term receivables offered during the winter months are collected during the spring and summer. This creates a seasonal peak in borrowing levels during the spring months.

The Company currently anticipates that no cash dividends will be paid on Water Pik Technologies common stock in order to conserve cash to fund the Company's future operations and growth. In addition, the terms of the Company's credit facilities prohibit the Company from paying dividends.

As of September 30, 2002, there were no material changes in the Company's contractual cash obligations and other commercial commitments from that disclosed in its Annual Report on Form 10-K for the year ended December 31, 2001. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations, Financial Condition and Liquidity" in the Company's Annual Report on Form 10-K for the year ended December 31, 2001.

Other Matters

Accounting Pronouncements

In July 2002, The Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This statement requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Statement 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. Management does not expect that adoption of this standard will have a material effect on the Company's consolidated results of operations or financial position.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 61, Amendment of FASB No. 13, and Technical Corrections." This statement clarifies guidance related to the reporting of gains and losses from extinguishment of debt and resolves inconsistencies related to the required accounting treatment of certain lease modifications. The provisions of this statement related to extinguishment of debt become effective for financial statements issued for fiscal years beginning after May 15, 2002. The provisions of this statement related to lease modifications are effective for transactions occurring after May 15, 2002. Management does not expect that adoption of this standard will have a material effect on the Company's consolidated results of operations or financial position.

In August 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." SFAS No. 144 retained substantially all of the requirements of SFAS No. 121 while resolving certain implementation issues. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001. Adoption of SFAS No. 144 in the first

quarter of 2002 had no impact on the Company's consolidated results of operations or financial position.

In June 2001, the FASB issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting, and broadens the criteria for recording intangible assets apart from goodwill. Under SFAS No. 142, goodwill and intangible assets that have indefinite useful lives will no longer be amortized but will be tested at least annually for impairment. Intangible assets with finite useful lives will continue to be amortized over their useful lives. The goodwill test for impairment consists of a two-step process that begins with an estimation of the fair value of the reporting unit. The first step of the test is a screen for potential impairment and the second step measures the amount of impairment, if any. SFAS No. 142 requires an entity to complete the first step of the transitional goodwill impairment test within six months of adopting the Statement. The Company adopted SFAS No. 142 in the first quarter of fiscal 2002. In accordance with SFAS No. 142, Water Pik Technologies identified two reporting units, the Personal Health Care segment and the Pool Products and Heating Systems segment, which constitute components of its business that include goodwill. The Company completed the first step of the transitional goodwill impairment

Edgar Filing: WATER PIK TECHNOLOGIES INC - Form 10-Q

test as of January 1, 2002 and has determined that the fair value of each of the reporting units exceeded the reporting unit's carrying amount, and no impairment was indicated. Had the non-amortization provisions of SFAS No. 142 been adopted for all periods presented, the Company's net income and net income per share for the three months and nine months ended September 30, 2001 would have increased \$343,000 and \$0.03, and \$982,000 and \$0.09, respectively.

In the fourth quarter 2001, the Company adopted Emerging Issues Task Force ("EITF") Issue 00-14, "Accounting for Certain Sales Incentives," and EITF Issue 00-25, "Vendor Income Statement Characterization of Consideration from a Vendor to a Retailer," resulting in the reclassification of certain customer promotional payments and cooperative advertising arrangements from selling expenses to a reduction in sales. Sales and selling expenses for all prior periods were restated to conform to this presentation. This reclassification resulted in a decrease in sales and selling expenses of \$1,653,000 and \$4,763,000 for the three months and nine months ended September 30, 2001. These reclassifications had no effect on reported operating profit.

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Reference is made to Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in the Registrant's Annual Report on Form 10-K for the year ended December 31, 2001. There has been no significant change in the nature or amount of market risk since year-end.

ITEM 4 CONTROLS AND PROCEDURES

Within the 90 days prior to the date of this report, the Chief Executive Officer and Chief Financial Officer conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in ensuring that all material information required to be filed in this quarterly report has been made known to them in a timely fashion. There have been no significant changes in the Company's internal controls, or in other factors that could significantly affect internal controls, subsequent to the date the Chief Executive Officer and Chief Financial Officer completed their evaluation.

23

PART II OTHER INFORMATION

ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K

- (a)
- Exhibits
- 4.1 Revolving Line of Credit Facility dated June 14, 2002, and executed on September 9, 2002, between Water Pik Technologies Canada, Inc. and BNP Paribas (Canada), as amended.
 - 4.2 Moveable Hypothec dated September 9, 2002, between Water Pik Technologies Canada, Inc. and BNP Paribas (Canada).
 - 4.3 Security Relating to Commercial Insurance dated September 9, 2002, between Water Pik Technologies Canada, Inc. and BNP Paribas (Canada).
 - 4.4 Amendment and Consent Agreement dated September 20, 2002, to the Restated Credit Agreement dated as of November 29, 1999, as amended, between Water Pik, Inc. and Laars, Inc., the Guarantors and Lenders named therein, and the JPMorgan Chase Bank (f/k/a The Chase Manhattan Bank), as Agent for the Lenders.
 - 4.5 Note and Security Agreement dated September 30, 2002, by Laars, Inc. in favor of Banc of America Leasing & Capital, LLC.
 - 4.6 Note and Security Agreement dated September 30, 2002, by Water Pik, Inc. in favor of Banc of America Leasing &

